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SINO-U.S. ECONOMIC RELATIONS: PROBLEMS AND PERSPECTIVES

by
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Sino-U.S. Economic Relations: Problems and Perspectives

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I. INTRODUCTION

Former President Nixon's historic trip to China in 1972 was only one of many steps on the road to normal Sino-U.S. relations, albeit a vital step. Prior to formal diplomatic recognition between the United States and the People's Republic of China (PRC) on January 1, 1979, the Chinese took decisive steps on their road to reformation. During the latter part of 1978, at the 3rd Plenary Session of the 11th CCP Central Committee, Communist China decided to embark on a reform program that would include opening China to the world and initiating structural changes within the economic and political systems. It seemed that China had finally realized the futility of the planned socialist system and isolationist policies.

In 1989, however, world perception of the sincerity and genuineness of the political leaders in China to actually carry out reform changed. The mass crackdown in Tiananmen Square in June, 1989, was a horrible enough act, in and of itself for most "Western" countries, as well as the rest of the world. What made the crackdown even worse in those perceptions was the fall of nearly all the Communist regimes in Eastern Europe later the same year. Congressman Dan Burton (Republican, Indiana) expressed a common feeling; namely, the turning of public opinion against the Chinese regime:

> For us to give any assistance to a continuing repressive regime like Communist China, when the countries of Eastern Europe are making dramatic progress toward democracy, is just ludicrous. If East Germany and Rumania can make democratic changes, why can't China do it.[1]

China not only shocked the world with its brutality but disappointed the anti-communist "winners" of the cold war, notably the United States.

The question of why China failed to aspire more heartily to democracy is interesting and will be debated in academic, political, and economic circles for a long time. The question however, presupposes that China's reforms that tended to relax centralized control of the economy would eventually lead to a fully functional market economy similar to those in "democratic" or "western" countries. Taking into consideration *perastroika* and *glasnost* in the late 1980's within the Soviet Union that paralleled China's modernization, most in the U.S. hoped that economic reform in China would lead to political reform. The Tiananmen debacle proved a tremendous disappointment.U.S. policy toward China, before Tiananmen, had sought ties that would counterbalance the U.S.S.R. Furthermore, the U.S. had sought China's support to reduce tensions in East and Southeast Asia, particularly Taiwan, Vietnam, Cambodia, and Korea. The Americans had also instigated a wide variety of exchanges to bolster political and economic reform and promote

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[1]Robert Pear, "Bush Hails a Thaw in China, Congress Is Skeptical," New York Times(NYT), June 12, 1990, A1:3.

human rights in China. And the U.S. had also endeavored to increase economic and commercial relations in order to facilitate China's movement toward a market-oriented economy.[2] The June massacre, however, swept away the expectations U.S. policy-makers had regarding China.

The Tiananmen debacle had another profound effect on U.S. China policy. The linkage between human rights policy and economic policies was reappraised by the U.S. administration, particularly President Bush. Having worked in China and obtaining a "close" relationship with China's leaders the President was as surprised as anyone by the events in Beijing. However, being closely associated with Deng Xioaping and the other leaders of China, perhaps Bush should not have been so shocked by such events.

Was this not the same regime that had recently enacted martial law and killed thousands in Tibet? Was this not the same regime that had recently prevented Fang Lizhi, the Chinese astro-physicist and human rights advocate, from attending a dinner engagement in Beijing at President Bush's invitation? If one takes a close look back in history, one realizes that Deng Xioaping supported the Anti-Rightist Movement in the late 1950's, and struck down the 1979 Democracy Wall movement. It should not have been so much a

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[2]See Lawrence Eagleburger's testimony before the Congress, Senate, Committee on Foreign Relations, U.S. Policy Towards China: Hearing before the Committee on Foreign Relations, 101st Cong., 2nd Sess., 7 February, 1990, p4.

surprise to anyone that this same regime would crush a similar democracy movement in 1989.

Then why were American China specialists, and especially those making policy, so astonished at Beijing's actions? Simply put, someone (or many people) were caught off-guard. Primarily, this involved mis-assessment of the goals of China's program known as the "four modernizations". China specialists might have better understood that "modernization" implied infinitely more than mere improvement in its agricultural sector, its industrial base, science and technology, and its defense. China no longer wanted to be, at best, a second rate power.

The problem deepened when China started to implement its reforms. Like so many other countries, the Chinese realized that the key to modernizing in all sectors would be economic improvement. Thus, economic reform would have to be the first place to start. It was only the prelude to further reforms that would presumably follow. Because of the scope and course that the reforms took, it is not difficult to see how so many China-watchers in the U.S. began to believe that China was, in fact, only shedding its socialist malaise and going "capitalist," without anticipating its further effects.

This would be a major mistake by the China-watchers, but not the only one. It was not realized how far the Chinese Government would go in brutal suppression of the opposition. Aware of the wide range of problems arising from Tiananmen, this paper will focus only on the economic aspects of the U.S.-China relationship. The major

question in contemporary U.S. China policy is whether or not Most Favored Nation (MFN) should be granted to the Chinese. Therefore, instead of asking, "Why can't China become a capitalist democracy?" It is better to ask what was China attempting to accomplish by "opening up" to the world, pursuing the "four modernizations," and using "market regulation" as the goal of its reform movement. Furthermore, how China views such issues as the Sino-U.S. trade relationship and finance(banking and loan) problems will enable decision-makers to use this information to their advantage in future policy planning.

The section entitled "China's Economic Revolution" examines China's economic reforms before Tiananmen, both agricultural and industrial, and where they were headed. It argues that China's economic reform did not specifically intend to achieve a capitalist market orientation. China was trying to achieve a better standard of living for its own people, taking fullest advantage of circumstances in China. The Chinese were eager to benefit their own country, regardless of labels or Western perceptions.

The following section discusses Sino-U.S. economic interaction. American policy aimed at assisting China to go capitalist; Chinese policy was to ask for assistance in national development, whether capitalist or not. This gap in perceptions cast doubt on the efficiency of U.S. policy in facilitating China's move toward a market economy. Did U.S. trade policy target those areas considered critical by China's leadership? Did the U.S. provide the technological and financial aid

needed to enhance China's reform? If not, what were the causes and reasons for the failure?

The next section looks at what China has done since that fateful event in Tiananmen Square. The purpose here is to determine if the Chinese reforms were permanently damaged, or if there are indications that the new leadership intends to continue with its basic modernization program. The road that China has taken since June, 1989, will determine future U.S. economic policies towards China.

The section on U.S. policy after Tiananmen considers the U.S. reaction to the Tiananmen incident as it has affected China's reform program. Here we analyze the two major sides, those that feel U.S. policy should be based on moral grounds and continue punishing China, and those who feel that the relationship is worth a major effort to preserve. Which U.S. attitudes prevail will have a great influence in determining China's future. Do economic restrictions help or hinder the Chinese people? Will restrictions coerce China's leaders into conforming to U.S. wishes?

Finally, the conclusion provides a coherent basis for any future U.S. policy decision. Policy recommendations are presented, depending upon fundamental choices made by the Chinese in determining their own future.

It is not the purpose here to compare the pros and cons of the free market systems versus planned economies. Both have their limitations. Though the collapse of socialist systems throughout East Europe may indicate the superiority of the capitalist system, it

cannot be denied there are differences within the capitalist systems of the world, for example the U.S. and Japan. There are indeed those who argue that the American system has already surpassed its peak and may take a back seat to the Japanese, though this argument is far from settled.[3] However, this is not the concern of this paper. Its scope is strictly limited to the issues surrounding the Sino-U.S. economic relationship.

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[3]See Paul Kennedy, The Rise and Fall Of The Great Powers (New York: Vintage Books, 1987), 677pp.

II. CHINA'S ECONOMIC REVOLUTION

The purpose of this section is to look at China's economic reform movement in an attempt to gain a better understanding of why certain policies were initiated and others were not. By understanding what China was attempting to accomplish through their reforms will hopefully enable U.S. policy-makers to formulate more appropriate policies based on U.S. interests in the future. It may also explain, in part, why the U.S. has reacted so adversely to the June, 1989, crackdown of demonstrators in Tiananmen square. The point being that U.S. china-watchers and policy-makers may have mis-interpreted the signs flowing out of Beijing.

China's agriculture was the first sector of China's economy to receive reforms. This was considered by China's leaders to be basic to broadening reforms to the rest of the economy. That is, if reforms failed in the rural sector, there would be no use in trying to spread reform to the urban centers.

After agriculture came industry. Industrial reforms were essential to link China to the global economic system, and hence the key area of U.S.-China economic relations. It is apparent that the entire modernization program was never intended to create a predominantly market-oriented economy as most in the U.S. had hoped. China's leadership attempted to justify newly introduced market concepts as still conforming to the socialist revolution. It is essential for future American policy decision-makers to understand

that China's leadership usually means what is says, and that seemingly rhetorical statements should not be passed off lightly in the future.

A. AGRICULTURAL REFORM

One of the first and most effective reform initiatives coming out of China involved the state increasing its procurement prices for agricultural goods in late 1979 and early 1980. This was perhaps the first price reform measure taken by the Chinese Government, in that it may have equated selling price with the cost of production. It was not price reform in the sense that prices were regulated by the market. Not only did the state increase prices paid to the farmer, but they also froze the quota requirements for mandatory delivery to the state. Farmers that produced above the required limit were allowed to sell that share of annual output on the open market, at what became a higher price than state prices.[4]

This new policy would become known as the household responsibility system and was adopted as a uniform national policy in 1983. The formalized system consisted of collectives assigning plots of land to peasant families to farm. The peasant families would then provide their share of taxes due the government, provide the required amount of products purchased by the state under the

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[4]Harry Harding, China's Second Revolution: Reform after Mao (Washington, D.C.: The Brookings Institution, 1987), pp101-102.

mandatory quota system, and pay the required fees owed to the collective. Then the above quota production could be consumed by the family, sold to the state at state prices, or sold on the open market.

The household responsibility system eventually provided for the abolition of the communes established under Mao, and transferred control to the production brigades.[5] Mao was contemptuous of the concepts of specialization and comparative advantage, and therefore favored the notion that every sector of society should be engaged in the same set of economic activities as all others. This would be reflected in the insistence that all of China's agricultural communes, which numbered 50,000 in the mid-1970's, should devote paramount attention to the production of grain, regardless of terrain and climate.

The establishment of the household responsibility system, however, eventually allowed the control over agricultural land to be transferred to smaller production brigades. Responsibility for agricultural services and local industry was frequently shifted to government agencies, collective enterprises, or even individual peasant households. This allowed the peasants to have a greater say in what and how much was produced. Thus, farmers could plant other crops than grain and choose appropriate crops for the environmental conditions. In other words, the agricultural reforms

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[5]Ibid., p103.

encouraged diversification; the peasants could produce industrial crops. The communes were being phased by 1983, and all were deactivated by December, 1985.[6]

In this way the reforms helped to establish a rudimentary form of rural industrialization. These new industries could be individual or collective, and included the raising of livestock, providing transport services to farmers, and other low level industrial goods. On its part, the state would try to provide rural transportation to help the distribution of goods. Through this rural industry, the government attempted to absorb most of the surplus labor in China's rural areas. The expansion of these alternative employment opportunities focused on a goal of decreasing China's rural labor from 85% in 1984 to 30% by the year 2000.[7]

The initial effects of the reforms were tremendous. Between 1978 and 1986 real farm family incomes increased 100 percent.[8] Average annual growth during the period 1979-84 was seven-point-seven percent, but dropped to four percent during the period 1985-88 (this would prove troublesome considering China's inflation rate of 25% in 1989). Furthermore, with rural industry excluded, the

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[6]See the note below Table B-2, Appendix B, in James T. H. Hsao, China's Development Strategies And Foreign Aid (Lexington: D.C. Health and Company, 1987), p147.

[7]Harding, p102.

[8]Congress, Joint Economic Committee, Agricultural Reform In The Soviet Union And China: Hearing before the Joint Economic Committee, 101st Cong., 1st Sess.,7 September, 1989, p13.

average monetary output of an agricultural laborer increased from 660 yuan in 1980 to 840 yuan in 1986. Perhaps most important, the average peasant income grew from 134 yuan. in 1978 to 424 yuan in 1986 while average consumption grew from 132 yuan in 1978 to 352 yuan in 1986.[9]

Though the (then) new reforms gave China's peasantry new hope and financial improvements the agricultural reforms would have their share of problems. One particular concern of the government's was low agricultural investment. For years the peasant's had worked on collectives under state plans without property rights or ownership. Though the household responsibility system had basically leased property to the peasants for cultivation the peasants were still reluctant to invest in land they did not officially own; there was no guarantee that the state would not take the land back at a later date. Thus, in 1984 the state pledged to leave the division of land unchanged for 15 years to give farmers an incentive to invest.

Another problem that arose had to do with the increased state procurement prices. Though the state was paying higher prices to the peasants, and the peasants were selling more to the state, the resultant rising cost of agricultural products was not passed on to the consumer. Consequently, a rapid increase occurred in state subsidies for agricultural products. To solve this, in 1985 the state would no longer issue mandatory quotas. Instead, the state replaced

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[9]Harding, p274.

mandatory state purchases of grain with the voluntary procurement contract system. This consisted of the state setting targets for procurement of a small number of products, such as grain, cotton and other important industrial crops, and offered to sign purchase contracts for those products with the peasants. The government also reduced the price controls on some agricultural products including meat, eggs, and vegetables. The quick result was to decrease grain production by six percent and the average price rose nine percent.[10] The government then attempted to increase incentives for grain production, such as giving farmers scarce inputs like fertilizer and diesel fuel at subsidized prices. Tax reductions, and low interest loans were also included to get farmers to grow grain.

Another interesting point concerning agricultural modernization in China was a contradiction in the state's stated priority in the sector and the actual investment the state plans called for in agriculture. Over the years, state budget expenditures dropped from 13.6% in 1978 to 8.3% in 1985, and to a low of about five percent in 1988. The total amount invested in the Sixth Five-Year Plan (1981-1985) was 30% less than in Fifth Five-Year Plan (1976-80).[11]

Summarizing, it is apparent that China made legitimate attempts at modernizing its agricultural sector. However, the reforms have

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[10]Ibid., p72.

[11]Congress, Joint Economic Committee, p34. This differs from Harry Harding's data indicating state investment dropped from 10.6% in 1978 to 3.3% in 1986, see Harding, The Second Revolution, p107.

not been without major problems and the benefits derived from them began to subside in the mid-1980's. According to Harry Harding, the Chinese Government needs to increases its investment in agriculture or it will be difficult to sustain the rates of growth seen early on in the reform movement. Furthermore, China may continue to have shortfalls of grain because of the abandonment of mandatory quotas for grain. Further price reform, such as removing subsidized consumer prices, may be needed to improve grain production.

B. INDUSTRIAL REFORM

Soon after the death of Mao, the post-Mao leadership conducted a review of China's economic performance during the period from 1957 to the 1970's. Attention had to be extended to the industrial sector of the economy. Two major findings were the result. First, China produced chronic shortages of useful goods and chronic surpluses of useless goods. This was in part a result of low labor productivity. The second major problem was poor capital productivity through technological stagnation of the engineering kind.[12] For example, the Chinese estimated that fully 60% of the technology employed in their industry in 1980 was completely obsolete, and the rest was in dire need of upgrading.[13] It was

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[12]Jan S. Prybyla, "A Broken System," in The Broken Mirror: China After Tiananmen, ed. George Hicks (London: St. James Press, 1990), p182.

[13]Harding, p33.

determined that the principle problem was systemic. That is, the problems resulted from the central administrative command planning system because that system did not address problems of scarcity.

Thus, to address the problems inherent with scarcity, China's economy would be carried out on the basis of public ownership while at the same time using the supplementary role of "regulation" by the market mechanism.[14] This would be one of the guiding principles for future economic reforms. Only the distribution of national revenue, investment in capital construction, and rationing of important products would be included in the unified state plan and be put under the direct control of the state. Thus, large enterprises would continue to have limited independence. However, medium and small enterprises, which had a closer link to the market, would be granted more independence, but not total independence. The Chinese would also regulate the rate of growth.

To achieve greater independence for the small to medium sized companies, the Chinese extended, to various degrees, regional, and especially, enterprise's autonomy and make systematic use of the regulation function of the market. For example the early reforms of late 1978 created first, production teams, then individual families, which were assigned state production quotas and allowed control

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[14]*Wen Wei Po* in Foreign Broadcast Information Service-Daily Report, China (hereafter referred to as FBIS), August 31, 1981, W4.

over the disposal of any above quota production in the market, very similar to the household responsibility system. Some of the state enterprises were also allowed to retain a share of the profits and to sell independently their above quota portion. Individual markets were opened to allow for distribution. As with grain production, state revenues declined as a greater share of the profits were withheld. However, investment at the local level rose.[15]

Another factor important in achieving better and more useful goods required planning and business administration departments to acquire the skill of manipulating economic levers with a view to inducing grassroots enterprises to engage in activities which met the requirements of the state plan.[16] The economic levers to be used included the price mechanism; or as the Chinese put it:

> Use the law of value as a regulator to regulate the supply and demand relationship of all kinds of products through the price mechanism so as to ensure proportional development of the national economy.[17]

Thus, government institutions would begin to manipulate the economic levers that the market regulated in a capitalist economy. This may sound like a far cry from economic reform, but as Xue Muqiao, a Chinese economist, put it:

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[15]Harding, p71.

[16]"Xue Muqiao On Economic Management System Reform," FBIS, February 24, 1982, K12.

[17]Ibid.

> To give enterprises greater autonomy and to let the market forces perform their regulatory function does not mean that the state may relax its supervision and control over economic life.[18]

Instead of putting all economic activities into the state plan, the State would use economic levers and legislation to induce enterprises to engage in activities in compliance with the state plan. Xue justified this by stating that capitalist countries also supervised enterprise activities, but they used levers and legislation instead of a state plan. The key was to get China to begin concentrating production on goods that were needed and the quality of those goods. Chen Yun, the noted Chinese economist, summed it up:

> Since we are running socialist enterprises, we should pay all the more attention to whether or not the products are marketable, where the raw materials come from and how the enterprises should be operated.[19]

Another huge problem of the command economy system, and perhaps inherited from the Soviet model, was over-investment in capital construction projects and an emphasis on the mandatory quotas of products that were, as mentioned earlier, useless. Thus, China's industrial reform was aimed at solving the problem of large deficits resulting from unproductive projects, stabilizing commodity prices, preventing inflation, and ensuring the overall stability of the economy. Therefore, instead of concentrating on high quotas and

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[18]Ibid., K15

[19]"Chen Yun Discusses Economic Strategy At Meeting," FBIS, March 9, 1982, W1-W2.

heavy industry as had been done in the past, China attempted to restructure the economy with the goal of coordinating the development of agriculture, light industry, energy, raw materials, machine-building and electronics industries, transport and communications, commercial services, as well as science, culture and education.[20] No longer would China rely on expanding capital construction and setting up new enterprises. Instead, China would use the full potential of existing enterprises, rectify and reorganize those existing enterprises, and raise the productive forces by carrying out technological transformation in a planned way.

One method involved a State Council decision on widening the commodities circulation channels between cities and rural areas and increasing the supply of manufactured goods to rural areas.[21] China needed to tap the labor resource of the 800 million peasants in order to produce goods for the masses. Key to the success was to provide peasants with low cost durable commodities as well as medium and high grade commodities which were mainly needed in the cities.

Another method used to curb the excessive expansion of capital construction was to exercise highly concentrated management over capital construction, further readjust the distribution relationship in the national income, and concentrate the necessary funds for

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[20]"*Renmin Ribao* Discusses Economic Readjustment," FBIS, January 8, 1982, K10.

[21]"*Renmin Ribao* Urges Opening Rural Market," FBIS, August 31, 1982, K15.

enhancing the major projects.[22] However, with all the talk of decreasing the emphasis in capital construction the actual share of national investment in capital construction occurring outside the state budget rose from 16.7% in 1978.to 61.5% in 1986.[23]

The other key element to achieving industrial modernization was China's "open door" policy. The main idea driving this policy was to acquire foreign capital and technology for investment because of the lack of Chinese capital and antiquated technology. The foreign capital and associated technology would be used particularly for investment in light and medium industries and agriculture. The emphasis would be on developing energy, transportation and telecommunications, raw materials, commodities for basic necessities, and, most importantly, goods for export. The Chinese would emphasize the export industry because only through exports would they be able to acquire the necessary foreign exchange to pay for borrowed capital.

However, opening up would prove to be tricky because of past emphasis on self-reliance. Thus, a number of articles appeared in the Chinese press to convince the cadres of the importance of opening up to receive foreign capital and technology for the modernization while at the same time justify that this would not impair China's ability to remain self reliant. For example, a Liaoning

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[22]"*Renmin Ribao* On Handling Economic Situation," FBIS, July 14, 1983, K13.

[23]Harding, p116.

Ribao editorial remarked, "using foreign investment does not go against the policy of self-reliance. Upholding the policy of self-reliance does not mean 'using less foreign technology or investment;' self-reliance means 'upholding national sovereignty in the main.'[24]

Similarly, a Yangchen Wanbao article stated:

> In implementing the open-door economic policies today, we are not reenacting history. Rather, being masters of a socialist country, we are acting on our own initiative to make use of foreign investment and importing technology in order to benefit the building of socialist material and spiritual civilization in our country.[25]

The fear of foreign influences was not limited to the fear of being dominated by foreign imperialists either. The Chinese also feared that opening up to capitalist countries would pollute and corrupt their society. Part of this problem manifested itself when foreign capital was invested in night clubs, hair salons, and other non-vital enterprises:

> The adoption of the open-door economic policies will definitely bring the ideology of capitalist societies, and the bourgeois way of life and customs will inevitably pound at our society. That is why we are strengthening ideological and political education and resisting the corrupt bourgeois way of life. This is a serious task of our struggle.[26]

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[24]"*Liaoning Ribao* Urges 'Bold' Foreign Investment," FBIS, December 9, 1981, S5-S6.

[25]"*Yangchen Wanbao* Discusses Foreign Influences," FBIS, February 24, 1982, K5.

[26]Ibid.

Therefore, when the SEZ's (Special Economic Zones) were established in 1979 they were not only used to bring in foreign capital and technology, but were the primary test sites for economic and social reform. They were also intended to serve as mechanisms for introducing, studying, and absorbing technology for application in a wider range of industries.

However, the ability of the zones to produce goods for export would remain a major priority. In the mid-1980s this would be reaffirmed when the Shenzhen SEZ was accused of making the majority of its profits off of mainland China instead of through exports. When asked about this case State Councilor Gu Mu replied:

> If the special economic zones cannot develop an export-oriented economy and make more contributions by earning foreign exchange through export trade, it will become meaningless to have them.[27]

The SEZ's consisted of four areas along the eastern coast, Shenzhen, Zhuhai, Xiamen, and Shantou. Obviously intended to encourage foreign investment in export projects, these areas were ideally suited because of the better than average infrastructure and access to port facilities. Another advantage to the location of the SEZ's were the proximity to Hong Kong, Macao, and Taiwan, which had proven themselves as successful traders on the global market.

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[27]"Gu Mu On Open Policy, Special Economic Zones," FBIS, April 11, 1986, K2.

Thus, the SEZ's would serve as bridges to link these areas with mainland.

To facilitate investment and make the plan work the Government promised to improve the infrastructure, provide a well-trained labor force, offer preferential tax rates and exemptions, and allow time for holidays in the zones. The enterprises in these zones were also given greater autonomy in that they were allowed to keep a greater share of profits, and management was allowed to pursue the interests of the company, to a point. In other words, China would expand the earlier industrial reforms similar to the household responsibility system to entire regions instead of individual families and small businesses.

Besides the provisions mentioned above, the PRC created a number of incentives which were intended to reward foreign investors. In 1981, China exempted import duties and industrial and consolidated taxes on advanced machinery equipment not available in China which was imported under contract by foreign partners. The enterprises receiving such benefits involved priority projects such as energy development and oil extraction, rail, road, and harbor construction, agriculture, forestry, livestock, crop cultivation, research and development, and health and medicine.[28]

Further measures were taken in 1983-1984 to reduce the scope of mandatory planning, grant greater autonomy to enterprises, and

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[28]"New Tax Rules To Encourage Foreign Enterprises," FBIS, February 2, 1984, p1.

decentralize the foreign trade apparatus. Apparently, the Chinese saw considerable advancement with the SEZ's and there incentives because the CPC Central Committee and State Council adopted a plan in 1985 to open up fourteen coastal cities and three coastal zones.[29] China also sought further reforms in the state finance system and changes in the wage system.[30]

Though China's adoption of the SEZ's, coastal cities and open zones, various tax breaks, and the reduction of overly centralized management helped to improve the standard of living of the average worker, there were basic problems the leadership had difficulty in dealing with. One particular problem was the pace that reform should take. Besides the problems with saturating Chinese culture too quickly with foreigners and their associated "pollutants," relaxing prices and increasing foreign imports resulted in high inflation and growing trade deficits.

To counter the adverse impact of reform, China would follow growth cycles with periods of retrenchment.[31] Many of the policies during these periods were antithetical to reform. For example, in periods of retrenchment China would slash the rate of investment,

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[29]The 14 coastal cities are: Tianjin, Shanghai, Dalian, Qinhuangdao, Yantai, Qingdao, Lianyungang, Nantong, Ningbo, Wenzhou, Fuzhou, Guangzhou, Zhanjiang, and Behai; the 3 coastal open zones are: Chang Jiang and Zhu Jiang deltas, and the Xiamen-Zhangzhou-Quanzhou delta area; see "Gu Mu On Opening Up, Reinvigorating China," FBIS, August 2, 1985, K9.

[30]Harding, p72.

[31]Ibid., p73.

decrease the rate of growth in the money supply, and reduce production quotas. Furthermore, as a result of a one-point-five billion dollar deficit in 1985 and a six-point-four billion dollar deficit in the first half of 1986, China placed restrictions on the ability of the "open" cities to conclude investment contracts with foreign firms, and limited access to foreign exchange.

However, as characteristic of the roller coaster ride of reform, urban reforms were restarted in the fall of 1986. China adopted a new labor system, relaxed price controls on some manufactured consumer goods, promulgated a draft law on enterprise bankruptcy, and experimented with capital markets by allowing a few state-run enterprises to be leased to individuals or groups of workers, or issuing shares of stock and forming a board of directors.

Besides having a difficult time in deciding how the pace of reform should proceed, there were basic obstacles to foreign investment The prospect of utilizing an abundant supply of low-cost labor proved to be wishful thinking. During the early stages of reform, enterprises did not have the authority to hire and fire as they pleased. Most of the labor had to be approved by local, regional, or even central institutions. Furthermore, most Chinese laborers were poorly trained and/or disciplined.

Foreign enterprises faced other difficulties such as the high cost of important inputs including land, housing, and office space. There was the low quality of Chinese components, uncertain availability of raw materials, difficulties in obtaining loans in Chinese currency, an

incomplete legal system, overburdened communications and transport systems, and convoluted lines of authority in the Chinese bureaucracy to contend with.

China, in good faith, would attempt to respond to these complaints. They would lower the cost of doing business by reducing land use fees, taxes, the cost of some inputs, and wage rates. They also promised to improved access to crucial inputs controlled by the State including water, electricity, communications, transport, and *renminbi* (Chinese currency) loans. China also tried to increase the efficiency with which the bureaucracy approved projects by establishing deadlines for such decisions and through creation of local service agencies that could expedite the review process. And,. again, they would guarantee greater authority over production plans, imports and exports, wages and bonuses, and employment dismissal of labor to the enterprises.

However, while increasing the number of institutions that could guarantee foreign investments and expedite the review process from 33 to 41, the individual guarantee limit of each institution was decreased.[32] Provincial limits were also cut, sometimes by half. Furthermore, the coverage of the guarantee dropped from 100% to 70%.

In addition, though tax incentives were provided in 1984, new taxes were imposed in 1985 that included levies on income earned

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[32]"PRC Changes Investment Guarantee Policies," FBIS, November 8, 1985, W1.

from services and consultations. A five percent income tax was imposed on foreign enterprises retroactive June 1, 1985. A 15% tax was applied to all offices receiving commissions, rebates, fees and other income for providing consultation, market surveys, liaison and other services to clients in China. As one Western diplomat put it, the tax regulations were "ambiguous."[33] Thus, it appeared to foreign investors that China was inconsistent in its policies and that the freedom to make a decision was more rhetoric than reality.

It is actions such as these that tended to discourage foreign investment and hinder China's overall reform policies. For example, even though the leadership offered to reform the trade system it did not necessarily result in greater freedom:

> The reform, is focused on freeing business enterprises from the administrative structure of the state and on decentralizing management powers. After the reform, the Ministry of Foreign Economic Relations and Trade will exercise unified leadership and specialized management over foreign economic activities and foreign trade in the whole country so as to perform the state's function of managing foreign trade work.[34]

It seems that the Ministry of Foreign Economic Relations and Trade (MOFERT) was the creation of one more centralized institution to "exercise unified" leadership over China's trade industry and not to facilitate enterprise autonomy.

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[33]"Reaction To New PRC Tax Regulations Reported," FBIS, May 17, 1985, W3.

[34]"*Renmin Ribao* On Reforming Foreign Trade System," FBIS, September 24, 1984, K13.

C. PRICE REFORM

The issue of price reform applies to both agriculture and industry, and seems central to achieving successful reform. Price reform would become another major avenue to achieve modernization. Because prices changed infrequently under Mao, relative prices became distorted; that is, prices may have been too low, fees for services too low or below cost, and prices of manufactured goods, such as steel, too high. Furthermore, prices were not allowed to vary due to transportation costs, seasonality, or quality.

As a result, prices on many commodities would be freed; some goods were put under the double pricing system; and prices on vital agricultural goods, such as grain, and raw materials would remain fixed. Yet, there was also reluctance to let the prices go completely free. Furthermore, if inflation was too high, all goods were subject to some form of control. For example, the State Council issued a Circular on Stabilizing Prices on January 8, 1982, because people had refused to buy goods through state commerce and planned distribution centers, yet were trading domestic commodities on the open and black markets.

At least China felt that even fixed prices must be based on quality.[35] Though this bears some resemblance to market regulation, quality alone did not set prices in the free market. However, it was a

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[35]"On Fixing Prices Based On Quality," FBIS, August 26, 1983, K10-K11.

step in the right direction. The Chinese also maintained that planned prices did not mean fixed prices. Major products bought by the State would have price controls, other products may have no price restrictions. More importantly, the Chinese leadership tried to simulate a market economy. That is, the state controlled prices to balance supply with demand and to equate price with equality.[36]

To correct the problems outlined above, Zhao Ziyang established a new pricing system consisting of fixed prices, floating prices, and market prices. The goal of the new pricing system was to reduce control by the state over production and pricing. The new system involved three channels for the distribution of commodities: mandatory planning (administrative orders), guidance planning (incentives by economic levers), and the marketplace (price control, if anything). Throughout the course of reform the number of commodities subject to mandatory planning was reduced.[37] For example, industrial products were reduced from over 500 products subjected to mandatory planning in the 1950's to eventually 60. In addition, agricultural commodities under mandatory plans were cut from 29 in 1984 to zero in 1985 with the adoption of the procurement contract system.

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[36]"*Renmin Ribao* Discusses 7 Years Of Price Reform," FBIS, February 10, 1986, K18-K23.

[37]Harding, p109.

The new price system was closely associated with the above distribution channels. Generally speaking, goods under mandatory planning had fixed prices. The number of industrial products sold at fixed prices was reduced from 256 to 29 under the new reforms. Likewise, the number of categories of consumer goods sold at state-set prices was reduced from 85 to 37, and the number of agricultural products with fixed prices dropped from 113 to 25.

Floating prices involved the state establishing a range within which prices could vary. The exact price was then determined by a contract between the producer and consumer or on the market. This system was first introduced in 1978 along with the first agricultural reforms and is associated with guidance planning.

Market prices are obviously connected to the marketplace, and consists primarily of small consumer goods and agricultural products What must be remembered about Chinese market prices is that the price, simply put, was allowed to fluctuate. In September, 1982, enterprises were allowed to set prices for 160 commodities, and in 1983, given similar authority for another 350 categories of goods. In 1985, with the end of mandatory purchasing, the prices of meat, fish, poultry, and vegetables were allowed to move freely on the marketplace.[38]

In summary, China's industrial reforms have changed the basic structure of China's economy and raised the standard of living of

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[38]Ibid., pp111-112.

urban workers. For example, the average urban wage grew from 614 yuan in 1978 to 1329 yuan in 1986. In addition, average consumption rose from 383 to 865 yuan.[39]

Yet at the same time it appears that industrial reform has not been sufficient to date. The onset of major inflation in 1987-88 along with corruption and a dissatisfied public led to the catastrophe of Tiananmen. In order for China to better their economic system they must increase competition among similar enterprises, provide the threat of bankruptcy for unprofitable producers, allow the emergence of markets for the factors of production (labor and capital), enhance price reform policies, and truly grant managerial autonomy.[40] Without such moves China's reform movement will not bring about the free market system so readily sought by the West. Therefore, if China's reforms are not indicating a move in such a direction, was a capitalist system ever a goal?

D. A SOCIALIST FRAMEWORK

The reform movement carried out by China after 1978 became central to every aspect of China's way of life; and the heart of this reform was the four modernizations. Modernizations were necessary in order to correct China's backward conditions and bring China to a

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[39]Ibid., p274.

[40]Ibid., p285.

level of development similar to those of the Newly Industrialized Countries in the 1970's.

Though the reform movement talked of opening up to the world and introducing market regulations the central theme of China's modernization was, and remains, socialist modernization. Market regulation would only be a supplement to the centrally planned economy.

Before the 3rd Plenary Session of the CCP in 1978 Deng Xiaoping began to send signals to the Party leadership of what was to come. Though Deng intended to introduce radical reforms into the socialist system(radical for China) it seems he had to tread carefully after the recent death of Mao Zedong so as to maintain power. Thus, Deng gave credit to Mao where it was due, and blamed the sorry state of conditions on the "gang of four." In a letter dated April 10, 1977, Deng wrote to the Central Committee:

> We must forever apply accurate and complete Mao Zedong Thought to guide the whole party, the whole army and the people of the whole country, to triumphantly press forward the cause of the party and socialism and the cause of the international communist movement.[41]

The main emphasis in the letter was that Marxism-Leninism-Mao Zedong Thought had basic principles that were useful. The problem with Mao's programs was that conditions at that time did not permit

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[41]"Comrade Deng Xiaoping Talks On Questions Of Correcting Party Work Style," FBIS, November 3, 1981, K1.

him to utilize these principles effectively, but now the proper conditions existed.

Deng would also expand Mao Zedong thought. On August 18, 1977, in his closing address to the 11th Central Committee Deng mentioned the "Four Principles" that must be continued:

> We must revive and carry forward the mass line, the fine tradition and style which Chairman Mao fostered...We must revive and carry forward the practice of seeking truth from facts...We must revive and carry forward the practice of criticism and self-criticism...We must revive and carry forward the practice of democratic centralism.[42]

Though the above quotations were primarily directed at correcting party work style in the aftermath of the Great Proletarian Cultural Revolution(GPCR) and the "wrong" policies under the gang of four, it underlined the communist ideology of the Party and indicated how the PRC leadership, particularly Deng, would intend to carry out future reforms. On November 27, 1978, during the 3rd Plenary Session, Deng would spell it out in no uncertain terms: "Marxism-Leninism-Mao Zedong Thought is the guiding ideology for our country to accomplish the four modernizations."[43] There would be no divergence from the socialist road.

Since that session the bureaucratic wheels of Chinese society would follow in Deng's footsteps. Prior to the Tiananmen "massacre"

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[42]Ibid., K2.

[43]Ibid., K1.

of 1989 (and afterward), there was little noted in the Chinese press that indicated any resemblance of China embarking on the "capitalist road." Instead, Chinese economists emphasized the development of a national economy in a planned and appropriate manner. The authoritative news agency, Xinhua, stated: "a socialist state like ours must carry out a planned economy on the basis of public ownership" while bringing in the supplementary role of market regulation.[44] The article attacked those cadres that believed a planned economy was "of little importance;" and that "these people regard the past occasional errors in building ideology and methods in planned economy as the very drawbacks of a planned economy and reflect planned economy as a basic principle of socialist economic development, which is incorrect."

The idea was to strengthen planning of the macroeconomy including the use of economic leverages such as prices, taxes, interest rates, and so forth, mentioned above, to guide (control?) the enterprises' economic activities. Without using a planned system an "anarchic situation" may arise "if these activities are not controlled by a state plan and if there is no regulation by economic leverages and no supervision by the various executive organizations." In essence, China would maintain a coordinated economy. If the economy was not coordinated in the proper way, and enterprises and peasants were allowed to do what they wanted, the state plan would

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[44]"Beijing Economists Stress Planned Economy," FBIS, January 5, 1982, R1.

be upset and may lead to stockpiling, inefficiency, and a general waste of resources.[45]

Another justification for stressing the planned economy was a fear of declining production in those areas vital to the state as a whole and the people's livelihood. In other words, the leaders did not believe that market mechanisms would insure the proper distribution of capital investment to those areas it was most needed. A Renmin Ribao commentator remarked:

> Although a good variety of products are produced under market regulation, their value constitutes only a very small portion of the total value of social production as a whole...they are not major products that are vital to the national economy and the people's livelihood. Thus, compared with the products produced and circulated according to plan, they are only in a secondary position...As to how large the scope of such products should be, it is defined by the unified state plan. Therefore, it should be clearly affirmed that the planned economies, by and large, form the main body of our economy. There should be no misunderstanding whatever about this.[46]

One interesting aspect of China's reform measures was how the market would be used. "It should be pointed out that making use of the market does not equate to market regulation"[47] in China. The Chinese were quite aware that "regulation" was when the means of production and quantity are set by price fluctuations in market

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[45]"*Renmin Ribao* Editorial Stresses Planned Economy," FBIS, February 26, 1982, K1.

[46]"*Renmin Ribao* On Reforming Planning System," FBIS, September 21, 1982, K2.

[47]Ibid., K5.

supply and demand; that activities of the market are guided by "spontaneous forces of the market." However, the PRC did not intend on allowing the market to make these determinations. Contrary to capitalist ideals, the Chinese intended to study the situation, determine what was needed and where, then provide goods and services through state plans. In other words, the state would interpret how the market would respond under the circumstances and plan accordingly:

> Although the enterprises implementing mandatory or guidance plans are also influenced by changes in prices, taxation and credits, these economic levers are all applied by the state in a planned way. Therefore, in the final analysis, they are controlled by state plans and are not regulated by the market.[48]

Another point was that the Chinese Communists did not feel that capitalism, or Western style economic systems, were compatible with the Chinese situation. It was mentioned earlier that Deng Xiaoping did not feel the circumstances were right when Mao controlled the reins to implement the reforms, but that the situation had changed. Thus, a recurring theme in dealing with China is that one must adapt to the situation, and that all situations are different. Therefore, one can not expect a socialist country to implement capitalist reform; socialist countries must implement socialist reform:

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[48]Ibid.

> We should not neglect the fact that the modernization we are striving to build is based on a socialist society rather than on a capitalist society. Therefore, not only are some concepts and theories of economics not suited to the economic reality in China, but some basic premises on which economies is based are in conflict with the socialist system.[49]

Even though agricultural reforms have been highly successful there are many aspects that still equate with a planned economy. Even though China's leaders acknowledge that planting is susceptible to local conditions the right to plant freely is not allowed. This would not allow for a proper relationship between "the state, the collective and the individual commune member." Thus, "carrying out planting in line with local conditions does not mean free planting."[50] In fact, agriculture should be guided by state plans, and the components of the agricultural economy should develop in coordinated manner.

Another startling discovery is that even the most renowned proponents of reforms, and those considered by the West to have encouraged steps towards a truly market economy, were stating the need to maintain a socialist system. For example, in 1986 Hu Yaobang, then General Secretary of the Chinese Communist Party, stated:

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[49]"*Renmin Ribao* On Applying Western Economics In PRC," FBIS, December 2, 1983, K12.

[50]"Planting Under Guidance Of State Plan Urged," FBIS, March 5, 1982, K22.

> Socialism has existed for several decades. However, in the history of mankind it is something new. It has also provided political confusion. Many may consider this proof of the lack of efficiency of socialism and deny its vitality. I am not of that opinion. Because it is something new, insufficiencies are unavoidable. When mistakes are made, one can try again. Lenin's ideas, for instance, are full of life. He said we would make some stupid mistakes. However, that is no reason for fear---after mistakes you can make a fresh start.[51]

In retrospect, it is hard to determine if such statements were meant to stave off critical attacks from more hardline Politburo members or whether or not they were actual policy. Considering what has transpired, it is conceivable that both may have been factors.

In summary, the Chinese leaders realized that something different was needed to pull China out from the abyss into which the Cultural Revolution had plunged them. Reforms were needed. But being good communists they would carry out a socialist revolution. The market mechanism would be secondary to the planned economy.

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[51] "*Die Welt* Interviews CPC Secretary Hu Yaobang," FBIS, November 19, 1986, G1.

III. SINO-U.S. ECONOMIC INTERACTION

The second aspect that needs to be considered in Sino-U.S. economic relations is how the two countries interacted in the economic arena. Even though it appears U.S. policy-makers misinterpreted Chinese intentions concerning the goal of reform, it seems logical that U.S. economic policy would concentrate on the areas identified by China's leaders as essential to modernization if it were true that one of the goals of U.S. policy was to enhance economic and commercial relations so as to move China toward a market economy.

Therefore, we should see steps on the part of the U.S. to transfer the necessary technologies and management skills to China to enhance infrastructure, agricultural production, and commodity production of basic goods. Though some of this has occurred, there are a number of signs that indicate that U.S. policy was short of the mark. To be sure, part of the problems arising resulted from China's inability to follow through with some reforms, and the failure to implement others necessary to entice foreign investment. On the other hand, it appears the U.S. has difficulty dealing with communist countries in general, China being no exception. Furthermore, during a period of declining competitiveness, increasing trade deficits, and protectionist lobbying, it is not too surprising that the U.S. reacted to a newly emerging international competitor in the way that it did.

A. TRADE AND RESTRICTIONS

After normalization in 1979, Sino-U.S. trade expanded enormously. Total two-way trade in 1979 was less than one billion dollars. This was primarily in textile exports to the U.S. and chemical fertilizer imports from the U.S. By 1983 trade had increased to $4.4 billion with an accumulated total for the period 1979-1983 of $22 billion. As of 1989, bilateral trade topped $12 billion.[52] The top ten Chinese exports included sweaters, petroleum, toys, rubber footwear, telephones, dolls, artificial flowers, stuffed toys, rubber/plastic soled footwear, and radio-tape players. The Chinese imported electronics, aviation equipment, transportation equipment, communications, construction materials, and received industrial technological transformation.

Besides the growth in trade, U.S. direct investment in China, between 1979 and 1989, involved over 950 ventures totalling over four billion dollars, making the United States the largest investor in China(this is only about one-point-five percent of U.S. total investments of $260 billion worldwide).[53] Chinese businesses have also signed over 627 contracts worth over $2.26 for U.S.

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[52]A number of articles were used to obtain these figures. For 1983 see "*Wang Yaoting* Views Sino-U.S. Trade Relations," FBIS, April 24, 1984, B1; for 1989 see "Retention of Trade Status With U.S. Urged," FBIS, April 4, 1990, p4, and Susumu Awanohara, "Rights or duties?" Far Eastern Economic Review(FEER), May 3, 1990, p43.

[53]"U.S. Urged Not To Suspend MFN Status," FBIS, April 23, 1990, 9; The figure of $4 billion differs greatly from an $8 billion figure reported by Nicholas R. Lardy, China's Entry Into The World Economy: Implications For Northeast Asia And The United States, (Lanham: University Press of America, 1987), p6.

technologies.[54] As one can see, bilateral economic relations have made a tremendous start. Needless to say, there are a number of problems plaguing Sino-U.S. economic relations. The major areas of contention include trade deficits and import restrictions.

A major problem with trade deficits, and one that lends a great deal of confusion to trade problems in general, is how the trade figures are derived. The United States counts goods from both China and Hong Kong when figuring trade totals with the PRC. China, on the other hand, counts only direct Sino-U.S. trade and discounts re-exports and re-imports from Hong Kong.[55] For example, in 1989 two-way trade totalled $12.1 billion excluding Hong Kong, with Chinese exports totalling $4.3 billion and Chinese imports totalling $7.8 billion. This would give China a deficit of $3.5 billion. However, the U.S. claimed a trade deficit with China of $3.7 billion because the U.S. government included Hong Kong's re-exports worth $8.5 billion(re-imports totalled $1.3 billion).[56]

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[54]"'Roundup' Urges Relaxation on U.S. Technology," FBIS, July 15, 1988, 8.

[55]See both Awanohara, p43; and "Retention of Trade Status With U.S. Urged," in FBIS, April 4, 1990, p4.

[56]Virtually all figures I found were inconsistent. For example, the "Retention of Trade" article lists Chinese Exports to the U.S. as $4.3 billion and imports at $7.8 billion, providing a total of $12.1 billion. Awanohara, "Rights or duties?" comes closest to this listing Chinese direct exports at $4.4 billion and imports at $7.9 billion; when including Hong Kong, Chinese exports total $12.9 billion and imports are $9.2 billion, giving the U.S. a deficit of $3.7 billion. However, this differs from Susumu Awanohara, "No more favours," FEER, April 19, 1990, p12, which put the U.S. 1988 deficit at $3.5 billion and the 1989 deficit at $6.2 billion. Yet the $6.2 billion figure compares with Carl Goldstein, "China needles US," FEER, January 24, 1991, p35, which put the '89 U.S. deficit at $6.5 billion and estimates the 1990 deficit with China at $12 billion.

This has repercussions in two ways. First, China emphatically resists large trade deficits mainly because they lack the foreign exchange to pay for them. They also tend to narrowly focus in on the bilateral relationship when discussing deficits. Therefore, even if they may have an overall surplus they will still point out bilateral deficit problems.[57]

This is directly linked to the second problem which also involves trade restrictions, foreign investments, and technology transfers(discussed below). Mainly, when the Chinese have a deficit with a particular country they will attempt to expand exports to that country while at the same time reducing imports, just as any other prudent nation would do(witness U.S.-Japan "trade-wars"). A typical Chinese response to a trade deficit with the U.S. is:

> If this state of affairs is not remedied, the quick development of trade between the two countries cannot be maintained.[58]

In textile negotiations(discussed in greater detail below) the Chinese continuously alluded to the trade imbalance(and other problems) to justify their position against U.S. textile restrictions:

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[57]China had an overall surplus of $8.1 billion in 1990, the first in 7 years, see Elizabeth Cheng, "Power to the centre," FEER, January 24, 1991, p35.

[58]"*Shijie Jingji* On International, Sino-U.S. Trade," FBIS, August 19, 1982, A4.

> Sino-U.S. [textile] trade is a part of Sino-U.S. trade as a whole. Thus, textile negotiations ought to take the overall situation of trade between the two countries into serious consideration.[59]

Closely linked with the trade imbalance, trade restrictions are the second major issue in Sino-U.S. economic relations. The Chinese feel that "there are undeniably many obstacles and difficulties in bilateral economic cooperation and trade", but that "fundamentally they arise from the fact that the United States has so far delayed changing its policy of discriminatory restrictions on trade with China."[60]

Furthermore, U. S. trade restrictions exacerbate China's problem because without trade they lose the capital to apply towards servicing their debt. From the U.S. perspective, the deficit has doubled the past two years in a row, and was justification for protectionist measures.

Interestingly enough, many in the U.S. agree with China's position. In an address given before a joint economic meeting Donald Regan, then U.S. Secretary of the Treasury, said:

> The United States will try to remove impediments obstructing the development of trade and economic relations between the two countries,[61]

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[59]"*Ta Kung Pao* Reports On Sino-U.S. Textile Talks," FBIS June 15, 1981, W8.

[60]"*China Daily* On Future Of Sino-U.S. Textile Trade," FBIS, August 28, 1984, B1-B2.

[61]"Bo Yibo, Regan Address Economic Meeting," FBIS, November 19, 1981, B3.

such as the abrogation of out-of-date legislation. Perhaps the key word here was "try."

The Jackson-Vanik amendment and the issue of Most Favored Nation (MFN) status for China is at the heart of the trade restriction issue. The Chinese state that the Sino-U.S. Trade Agreement signed in 1979 accorded one another MFN treatment. Furthermore, they argue, MFN in "legal terms" is an international commitment and the U.S. has no right to unilaterally carry out so called examinations.[62] The examinations referred to here are the U.S.'s consideration of China's emigration policy. Jakson-Vanik requires any communist country that applies for MFN to meet U.S. requirements on emigration; essentially, a free emigration policy. The PRC further argues that the first Clause in the first Item of the General Agreement on Tariffs and Trade (GATT) stipulates that signatories should grant MFN status to one another.

But MFN had already been granted to China in 1980. Why were the Chinese so upset? Primarily because China's emigration policies or the presidential waivers to Jackson-Vanik had to be reviewed annually. The Chinese felt this to be an infringement of their internal affairs and sovereignty. This issue would not only become exacerbated by the Tiananmen incident, but become the central issue in U.S. debate over economic policy with China, and will be discussed in more detail (see Section IV).

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[62]"U.S. 1974 Trade Act Discriminates Against PRC," FBIS, December 23, 1986, B2-B3.

Another major trade problem consists of U.S. protectionist measures on the import of Chinese textiles. When the first Sino-U.S. Textile Agreement was signed in 1980 only eight categories of Chinese goods were restricted from U.S. markets. By the end of 1986 that number had grown to 48. Those are only direct restrictions. China, in an attempt to appease U.S. textile manufacturers and avoid further restrictions, had unilaterally restricted 22 items under Voluntary Economic Restraints, at the demand of the U.S. no less. All in all, 90% of Chinese textiles had restrictions of one form or another by 1986.[63] Most of these restrictions had come in the form of Congressional legislation.

On September 7, 1984 the "country-of-origin-rule" was to go into effect. The rule stated that semi-finished goods imported for re-export must be substantially altered in order to put a different country label on the finished product. What this meant for China was that semi-finished textiles sent to Hong Kong for finishing and re-exporting to the U.S. would be charged to China's export quotas unless substantially altered. At stake were numerous contracts between Hong Kong and Guangdong province that effected 400-500 factories and up to 50,000 workers.[64]

Zhang Wenjin, then PRC Ambassador to the U.S., wrote a letter to the U.S. Government protesting the measure "which would create

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[63]"Sino-American Textile Talks Called 'Failure'," FBIS, December 2, 1986, B3.

[64]"*South China Morning Post* On U.S. Textile Rules," FBIS, August 15, 1984, W3.

further difficulties for China's textile exports," and that the new rules "constitute a clear violation " of the bilateral trade agreement and the Multiple Fibre Agreement.[65] The American Association of Exporters and Importers textile and apparel group considered the rule "a blatant new trade barrier."[66] Their main concern was the effect the rule would have on unfilled contracts. To alleviate this problem the U.S. extended the effective date to October 31, 1984, for those shipments ordered prior to August 3, 1984.

In 1985 the textile issue was reheated by the U.S. Trade Enforcement Act. This bill put additional restrictions on textile imports. Apparently, China's exports would be cut by 56%, a potential loss of $500 million.[67] In 1987 the U.S. obtained another agreement that cut the annual rate of growth by volume in Chinese textile exports from 19% to three percent. Furthermore, in 1990 the U.S. Senate passed another bill decreasing the growth rate to one percent (as of this writing it had not been signed into law). Particularly infuriating to the Chinese was that the bill applied to all countries except Canada and Israel.

Though the majority of these laws were probably aimed at Japan, South Korea, Taiwan, and Hong Kong, the Chinese are particularly touchy because textiles account for 38% of their exports to the U.S

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[65]"PRC Ambassador Protests New U.S. Textile Rules," FBIS, August 20, 1984,B2.

[66]"U.S. Businessmen Criticize Textile Import Rule," FBIS, August 22, 1984, B4.

[67]"PRC, Hong Kong React To Threat From Textile Bill," FBIS, July 9, 1985, B1.

[Ref. 68].[68] They feel that these restrictions will hinder their access to foreign exchange which is vital to their modernization efforts.

B. TECHNOLOGY TRANSFERS AND RESTRICTIONS

The other important factor in China's open door policy besides developing export industries was acquiring foreign technology. U.S. policy tended to compliment this goal. Though the United States' ability to influence Chinese developments was considered limited, it was felt that technology transfers could build ties between the two countries. This would also enhance China's strength vis a vis the Soviet Union. Furthermore, technology transfers could lead to important commercial ties and the eventual export of U.S. products. Finally, because China was a poor country, technology transfer could be an important element in humanitarian efforts.[69]

Another reason technology transfer would be crucial to relations was an eventual requirement by the Chinese Government that foreign ventures export or supply advanced technology in return for access to Chinese markets. China's lack of foreign exchange to purchase new technologies was part of the reason for this request.

In 1972 China was listed in category "Y"(of U.S. rules on technology export) which was severe restriction. In 1980 this was

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[68]Ibid.

[69]Congress, House of Representatives, Committee on Foreign Affairs, Technology Transfer to China: Hearing before the Subcommittee on International Economic Policy and Trade, 100th Cong., 1st Sess, 8 July, 1987, p5.

upgraded to category "P," which was "somewhat" restrictive. Finally, in 1983 China obtained category V, which meant China was considered a "non-allied friend."[70] In other words, China was to be considered similar to some of the NATO nations. However, China complained that because they were still listed as a non-market economy, they were discriminated against. For example, they are still unable to receive high-technology goods or those with military-civilian applications.

In 1979 a broad agreement, followed by 25 protocols implementing the agreement, was signed covering specific areas such as telecommunications, agriculture, space, environmental protection, transportation, and student/scholar exchanges.[71] Such contacts have facilitated commercial transactions and political contacts. The presence of 17,00 Chinese students and scholars in U.S. universities has been one of the most effective forms of transfer.

Further agreements have been reached In August, 1984, the U.S. and China sign a technological cooperation agreement whereby the Bureau of Reclamation and the Department of the Interior would provide technological help to design and construct the Three Gorges Dam on the Yangtze river.[72] However, construction had not started

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[70]"'Roundup' Urges Relaxation on U.S. Technology," FBIS, July 15, 1988, 9.

[71]Congress, Technology Transfer, p11.

[72]James T. H. Hsao, China's Development Strategies And Foreign Trade, (Lexington: D.C. Health and Company, 1987), p70.

as of May 3, 1991. The agreement also established work programs in electronics, telecommunications, machine building, and building materials.[73] In the workshops, Chinese representatives would outline priority areas and U.S. representatives would identify U.S. companies with expertise in those areas. Furthermore in 1985, an Agreement on Nuclear Cooperation provided the legal framework for U.S. companies to sell nuclear material, equipment, and services to China.[74]

Because technology transfers have been only partially successful they have created one more area of contention between the two countries. It appears that the main problem, from the U.S. perspective, is that China is a socialist nation. Though United States' China policy is predicated on the assumption that closer relations are better, sanctions must continue to be exercised in areas of advanced technology.[75] Though this policy has had some success, such as China playing an increasing constructive international role, and bilateral trade had become significant, the reasons for caution have not been eliminated. China was still considered a potential adversary; China had an alien ideology; and China's political system was unpredictable. Furthermore, there was a sense that China was potentially another

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[73]Congress, Technology Transfer, p71.

[74]Qingshan Tan, "U.S.-China Nuclear Cooperation Agreement," Asian Survey, Vol. 29, No. 9 (September, 1989), p870.

[75]Congress, Technology Transfer, p6.

NIC (Newly Industrialized Country) rapidly upgrading its production in technology and aggressively seeking international markets. There was fear that China could eventually become more powerful than Japan or South Korea with respect to technology transfer.

The most troubling aspect was what would China do with the technology received vis a vis the military, particularly in arms sales. The Chinese considered the sale of arms as just another means of acquiring foreign exchange to help its modernization efforts. The U.S., however, saw military arms sales as a way to stabilize (or destabilize) the geostrategic balance. Thus, when China became a major player in the international arms sales business, the U.S. was concerned.

The Iran-Iraq war facilitated China's arms sales. Prior to the war, most Chinese arms went to the Asian buffer states of North Korea, North Vietnam, and Pakistan. Once China became involved in the Middle East market, their sales boomed, ranking fifth in the world, after the Soviet Union, the U.S., France, and the United Kingdom.[76]

Chinese arms sales in the region increased dramatically during the period 1980-1987. The U.S. Arms Control and Disarmament Agency published data indicating that 80% of China's arms deliveries from 1982-1986 went to the Middle East. Arms sales to Iran and Iraq comprised 74% of China's total. Though the sales included

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[76]For a detailed look at Sino-U.S. military relations see Eden Y. Woon, "Chinese Arms Sales And U.S.-China Military Relations," Asian Survey, Vol. 29, No. 6(June 1989), pp601-18.

ground equipment such as tanks and artillery, the primary concern involved China's sale of the HY-2 Silkworm missile. These were anti-ship weapons and posed a potential threat to U.S. war ships operating in the Gulf. Exacerbating this, it was discovered that China had sold the CSS-2 intermediate range ballistic missile to Saudi Arabia in March, 1988, there were potential plans to sell Syria the M-9 short range ballistic missile that same year (June), and Egypt was a growing customer. Besides the Middle East market, China's continued sales to Pakistan, and the growing sales to Thailand did not help. The U.S. saw Chinese arms sales as destabilizing these regions. It did not help matters when China disputed the sales to the Middle East, then eventually remarked that "some Chinese-made arms may have made their way to the Persian Gulf" through the complicated international arms market.[77]

The Chinese, however, felt that the U.S. criticism of Chinese arms sales was hypocritical. As Foreign Minister Wu Xueqian put it:

> Whenever China sells weapons, China becomes the newsmaker. How about the weapons flying over the Gulf? There are many kinds of them... these are not Chinese weapons. Why is it that some people always harass China with this so called issue?[78]

The point should be well taken. Why are U.S. weapons sales to these areas stabilizing whereas Chinese weapons are not? Could an

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[77] Ibid., p609.

[78] Ibid., p611.

underlying factor be that the Chinese are taking a good share of the international arms market away from the number one seller, the United States? This may be partly true, but the fact that Chinese Silkworms may end up attacking U.S. warships did not set well in the Pentagon.

In March, 1988, both countries took steps to solve the problem. The U.S. State Department lifted its freeze on technology exports to China in return for Chinese reassurances that it would take steps to stop delivery of the Silkworms. China also pledged to support an effort to get Iran to accept the U.N. Resolution 598, which would call for a cease fire to the war. This may have settled the Persian Gulf problem, but what about China's sales to other countries such as Saudi Arabia, North Korea, Pakistan, and the Khmer Rouge in Cambodia (thought to be supplied through the Thailand connection).

In the summer of 1988 Secretary of State George Schultz visited Beijing to discuss these matters. Shultz remarked after the visit:

> The Chinese told me that they had not made any sale of ballistic missiles to a country other than Saudi Arabia...As for ballistic missiles in general, we didn't come to any agreement about it, but I think it has been worthwhile to talk about it, and I am sure that the subject will continue to be an important one on our agenda.[79]

In September Defense Secretary Frank Carlucci, while visiting China, was told that future sales would be "very prudent and very

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[79]Ibid., p614.

serious." Furthermore, the Chinese promised to behave in a responsible way. The Chinese also promulgate three principles on arms sales:

> China is a responsible country. We always assume a serious, prudent, and responsible attitude toward the military products export question. In this regard, we strictly adhere to three principles: First, our military products export should help strengthen the legitimate self-defense capability of the countries concerned; second, it should help safeguard and promote peace, security, and stability in the regions concerned; and third, we do not use the military sale to interfere in the internal affairs of other nations.[80]

Finally, the U.S. acknowledged China's right to make arms sales decisions, but retains the right to express concern when U.S. interests are threatened.

Another problem regarding technology transfer occurs from private industry doing business in China. One associated problem are long negotiation periods.[81] For example, the company Wang Laboratories, negotiated for seven years until an agreement was reached. In another case, McDonnell Douglas negotiated over a ten year period. Finally, the recent satellite's released to the PRC for launching were initially begun in the 1970's. Then, there are the numerous other difficulties of doing business in China mentioned

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[80]Ibid., p607.

[81]Congress, Technology Transfer, p10.

earlier that prevent foreign investment, and hence, technology transfer.

Probably the most problematic area of technology transfers deals with dual-use technologies and the U.S. bureaucracy that overseas such transfers. Advanced dual-use technologies and arms can be exported to China on a case-by-case basis, depending on the nature of the technology, the Chinese recipient, conditions of the sale, and other factors. As it implies, this process is highly complex, difficult to administer, and can yield to inconsistent decisions and time delays.

U.S. industries are critical of the process, citing lengthy reviews, and lost contracts. Most countries only take a few weeks while the U.S. could take months or even years to approve a contract. Furthermore, the U.S. is the only country that unilaterally imposes controls on items not listed in COCOM (Coordinated Committee).

Primarily, the U.S. controls exports on computers, telecommunications, precision instruments, and advanced manufacturing equipment. The "green zone", in which items are likely to be approved, covers 30 categories. In 1987 the green zone was increased, raising the data processing rate for computers from 155 to 285. The increase provided an individual category for disc drives, allowed the export of higher capacity computer chips, and increased value limits on servicing equipment.

Above this green zone are products that would make a direct and significant contribution to six critical military capabilities. These include nuclear weapons and delivery systems, Anti-Submarine

Warfare, intelligence collection, power projection, Electronic Warfare, and air superiority. Interestingly enough, 50% of such cases went to COCOM in 1985 but only 20% went in 1986.

Thus, when a product falls into a yellow (may be approved) or red zone (almost never approved), there is a review period by the Department of Defense (DOD). Furthermore, there appears to be no distinct cut off point between the yellow and red zones. Thus, the Department of Commerce (DOC) may be pushing for a contract in what it feels is a yellow zone case whereas the DOD is stating the product falls into the red zone.[82]

According to Section 10(g) of the Export Administration Act, there is a process for settling such disagreements. This process, however, which culminates in an appeal to the President, is rarely involved. Instead, controversial cases bounce back and forth between the DOC and DOD for months or years. Furthermore, the statutory time limits are not adhered to. It has been estimated that hundreds of millions of dollars worth of exports have been lost to these delays.

Needles to say, the difficulties associated with technology transfers have not thoroughly satisfied the leadership in Beijing. Commenting on President Bush's election victory, Fei Xiaotong, a Chinese sociologist, felt the help from the U.S. appeared great, but was in actuality, very little. Fei said the U.S. should give China more

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[82]Ibid., pp19-28.

technology transfers and increase its investments, a sentiment felt by many of China's leaders.[83]

China also feels that the U.S. uses technology restrictions to compel them to conform to U.S. policies. In March, 1988, the United States was considering relaxing restrictions on exports of high technology equipment to China because they had finally stopped sending "Silkworm" missiles to Iran.[84] However, later that summer, it had been determined that China had not stopped those sales. The Senate (97-0), therefore, adopted a proposal to re-examine the potential sales of arms and technology transfers to China.[85] The Bill was approved 80-16, asking President Reagan to "reassess relations with China if Beijing does not stop selling missiles to the Middle East."

Restrictions on technology transfers are also viewed as a U.S. attempt to hinder China's modernization. However, many of the transfers are through direct and/or joint investments which U.S. businesses complain are hindered by China's laws. Fortunately, both sides agree that their should be mutual cooperation in these areas. Gu Mu, China's Minister of the State Administrative Commission on Import and Export Affairs and Foreign Investment Control Commission, states: "We want to increase trade and economic

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[83]FBIS, November 28, 1988, p8.

[84]David K. Shipler, "U.S. Informs China High-Tech Exports Could Be Widened," NYT, March 10, 1988: A1; 1.

[85]"Senate Criticizes the Chinese On Missile Sales in Mideast," NYT, July 28, 1988: A8; 6.

cooperation with foreign countries on the principle of equality and mutual benefit."[86] Likewise, then U.S. Deputy Secretary of State Walter Stoessel remarked:

> The U.S.-China relationship, like all relationships between equal, sovereign nations, should be guided by the fundamental principles of respect for each other's sovereignty and territorial integrity and non-interference in each other's internal affairs.[87]

C. FINANCIAL AID AND ADVERSE CONDITIONS

A final aspect to look at are those involving financial matters. As mention earlier, without foreign capital, mainly hard currency, China is unable to make investments within the country and/or unable to pay debts. The U.S. has a number of promotional programs that support trade with and technology transfers to China.

The Foreign Commercial Service in the Department of Commerce provides information and assistance to American businesses and helps potential Chinese buyers learn about U.S. goods and services. The Dalien Management Center, supported by the DOC, provides a training program for Chinese managers. The Overseas Private Investment Corporation (OPIC) has insured over 20 U.S. investments in China.

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[86] "Gu Mu Calls For Expansion Of Foreign Trade," FBIS, October 22, 1981, K3.

[87] "U.S.-China Trade Council Views Trade Expansion," FBIS, June 2, 1982, B1.

However, the Export-Import (Ex-Im) Bank's programs are comparatively limited because it is guided by the principle that the private sector should finance exports unless the national interest is involved or a competing foreign investor is assisted by a national government. Even before Tiananmen both the Ex-Im Bank and OPIC programs were being scaled back due to budgetary constraints. Moreover, there was no official U.S. aid program vis a vis China.

Since there was no formal aid program to China, and because of opposition to use "mixed credits," low cost programs were a vital tool for the U.S. Government to support the early stages of projects. One such program was the Trade and Development Program. This program provided project planning services, including feasibility studies, and had yielded great returns. For instance, a $440,000 TDP feasibility study of a hydropower project led to $20 million in U.S. exports.

Because of the poor performance on behalf of the U.S. to officially help in the financial arena, China was resentful. The other two major sources of financial aid to China involve the World Bank and the International Monetary Fund (IMF). Because of the significant role the U.S. played in these institutions China viewed the actions of the IMF and World Bank as a United States' action. In other words, these institutions were directly linked to Sino-U.S. relations.

One aspect of China's concern was the inability of developing countries to service debt and become developed without some form of "new" economic order (China considers itself the largest

developing country). Regarding a summit of the "Seven Industrial Powers" Zhao Ziyang said he hoped the summit would "put emphasis on the problem of the North-South economic disparity in the world."[88]

Because the IMF and World Bank are the primary institutions that raise funds for financial assistance to the developing countries it is up to these institutions to change the economic disparities between the "haves" and "have nots." Wang Bingqian, then Chinese State Councilor and Finance Minister, identified the major obstacles before an IMF-World Bank meeting:

> Intensified trade protectionism practised by a number of the developed countries, their reduction of official development aid, and rising real interest rates have made it hard for the developing countries to overcome their economic difficulties.[89]

The Chinese bitterly criticized the U.S. for its irrational monetary and fiscal policy while enjoying the benefits of a helpful economic relationship on the eve of Tiananmen. With the outbreak in June, 1989, in Beijing, U.S.-PRC economic relations took on an entirely different tone.

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[88]"Zhao Briefs Sakurauchi ON PRC's Economic Growth," FBIS, April 29, 1983, D1.

[89]"Wang Bingqian Addresses IMF-World Bank Meeting," FBIS, September 26, 1984, A3.

IV. CHINA AFTER TIANANMEN: WHAT NEXT?

Though the first chapter indicated the course China's modernization was taking we must address the situation after the bloody crackdown in Tiananmen square. Many have said that the incident proves that China's leadership does not want to lose power, or that the democracy movement was only temporarily crushed. However, the direction that China has taken will be crucial for future U.S. policy decisions. Thus, we must determine if a substantial alteration in China's reforms have occurred since June, 1989.

Perhaps the most crucial aspect in determining which direction China will go depends upon the person in power. As a result of Tiananmen Zhao Ziyang was replaced by Li Peng, notably more conservative with respect to reform. Thus, it becomes important to keep track of the leadership within China in order to obtain some grasp of the future course.

In China's Second Revolution, Harry Harding described what he called the radical reformers and the moderate reformers.[90] The radical reformers included Hu Yaobang (served as General Secretary of the CCP from 1982-1987), Zhao Ziyang (recently resigned as General Secretary), Hu Qili, Tian Jiyuan, and Wang Zhaoquo (the last three being younger leaders appointed to Party Secretariat in mid-

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[90]Harding, pp80-1.

1980's). They supported more sweeping reforms at a faster pace, and were reported to favor some political relaxations.

The moderate reformers included Chen Yun (Chinese Economist), Li Peng (current Premier), Peng Zhen (Chairman, National Peoples Congress Standing Committee), Hu Qiaomu (ideologist in the Politburo), and Deng Liqun (member of Secretariat with overall responsibility for propaganda). They support a smaller range of reforms at a much slower pace. In fact, it would be more appropriate to call them "modernizers" because they do wish to improve China's backwardness, but are not willing to do this at the expense of their hold on power. The role of Deng Xiaoping would be to balance the two factions, protecting the radical reformers to some degree, but as Tiananmen points out, will not forego the Party's power.

Interestingly enough, Jiang Zemin, the new General Secretary, is not listed in either of the above groups. This could lead one to believe that he is perhaps a "puppet" of Deng, and that he wields little, if any, power. On the other hand, Jiang may have power due to the fact that he has Deng's trust. At any rate, it now becomes more important to pay close attention to what is said in China, and by whom. For example, two relatively younger Party members were elevated to the level of Deputy Prime Ministers. Zhu Rongji, former Mayor of Shanghai, and Zou Jiahua, the head of the State Planning Commission, were given the new posts in April, 1991. Zhu was denounced as a rightist in 1957, and is known to favor broader

reforms. Less is known about Zou, but is also considered a plus for the reform faction. It has even been rumored that the elevation may indicate the eventual removal as Li Peng as Premier. Personnel shifts, however, are not the only indications of continued reform.

A. HINTS OF REFORM

Shortly after the crackdown, Deng Xiaoping remarked:

> Reform and opening up must not be changed. We should stress that they will remain unchanged for several decades. If we want to think of changing, it must be after the realization of the four modernizations.[91]

In October, 1989, Deng made further steps to reinforce China's desire to reform by separating Zhao Ziyang's personal mistakes from the "correct" ideas of reform. Deng went so far as to have the question on Zhao's future shelved for two years. Deng remarked, "Zhao Ziyang supports reform and the open door policy."[92]

Jiang Zemin, the new Party General Secretary, explained China's position on the whole affair:

> The essence of the matter, however, was that some individuals plotted an overthrow of the Communist Party leadership and the socialist system in China under the pretext of opposing corruption and used the students to achieve this aim of theirs.[93]

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[91] "Deng Urges New Leading Body to Grasp Reform," FBIS, June 28, 1989, 13.

[92] "Deng Seeks to Curb Anti-Zhao Campaign," FBIS, October 30, 1989, 28.

[93] "Jiang Zemin: 'Incident' 'Much Ado About Nothing,'" FBIS, June 6, 1990, 7.

In the summer of 1990, Beijing appeared to be taking positive steps. There was talk of converting state owned companies to joint stock concerns. Li Yining, economics professor of Beijing University and former advisor to Zhao Ziyang, was allowed to say that China needed to "develop the securities market as a way of freeing itself from the current financial predicament." Beijing reaffirmed the continuance of the contract system.[94] Furthermore, Jiang Zemin hinted at continued reforms by stating that "reform has not caught up."

Other positive steps were seen in 1990. The 1979 Chinese-Foreign Equity Joint Venture Law that was promised, but failed to appear during a 1989 session of the NPC, was finalized for promulgation at a 1990 session in order to reinvigorate the declining interest of foreign investors. Efforts were also accelerated to complete a copyright law. China began speeding up preparations for labor laws. China requested occasional assistance from the World Bank, the United Nations, and foreign experts to draft laws to regulate companies, banks, railways, and unfair competition.[95]

Furthermore, Jiang Zemin decided it was time to release Fang Lizhi, the astro-physicist and democracy advocate who had been staying in the American Embassy since June, 1989. Jiang had decided that the situation would only continue to cause strain in the

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[94]"Revival of Zhao's Reformist Ideas Said Considered," FBIS, July 20, 1990, 16.

[95]Jerome Alan Cohen, "Tiananmen and the Rule of Law," in The Broken Mirror, p330.

Sino-U.S. relationship, and it would be best to release him. Besides, Fang was a "dead tiger" and it would be unlikely for him to create trouble in the future.[96]

Another positive step was taken in October, 1990, when the Chinese Academy of Sciences resumed ties with the American National Academy of Sciences and the American National Scientific Foundation after suspension in June, 1989.[97] This demonstrates a desire to continue improvement in China's technology and hence, modernization.

More recently, China enacted measures that would seem to indicate a move toward fair competition among domestic industry. Effective January 1, 1991, China scrapped its export subsidies. The move was primarily designed to curb growth of the independence of regional government's and to promote heavy industry ahead of light industry. Furthermore, China would begin an overhaul of the internal allocation of foreign exchange earnings. Again, this was to reduce the deficit plus the introduction of a unified trade policy.[98]

At first glance these measure would seem to indicate a period of retrenchment. However, curbing the independence of regional governments restores much of the dissipated power of the central authorities. It may be more directed at controlling the prevalent

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[96]*Cheng Ming* in FBIS, July 3, 1990, pp16-18.

[97]*Xinhua* in FBIS, October 11, 1990, p4.

[98]Elizabeth Cheng, "Power to the centre," FEER, January 24, 1991, p34.

corruption associated with regional independence. Reducing subsidies will also require enterprises to become more innovative and efficient, especially if bankruptcy laws are promulgated. The scrapping of subsidies ended all policy privileges for state enterprises in Guangdong, Fujien, and the SEZ's. They must now compete on a more equal footing with northern industries. The removal of export subsidies may also enhance China's entry into GATT. Finally, the scrapping of subsidies will save the central government a substantial amount. For example, direct and indirect subsidies to state enterprises in 1990 were 106.4 billion *renminbi*.

The recent measures also effected the foreign trade agencies' profit margins. China's foreign trade agencies can now retain 70% of their earnings from electrical and capital goods, 50% from other products (10% to local government, 40% to companies), and export-processing enterprises can keep 90% of their earnings.

It seems that the current trend is very similar to that of the early 1980's. Much of the same rhetoric is being used, and the priorities of granting greater autonomy to enterprises and the consideration of price reform continue. Ma Hong, Director General of the State Council's Economic, Technological, and Social Development Research Center wants to push China's economic construction forward:

> However, the tasks for reform are from being completed: The new economic structure has not been full-fledged; enterprises (especially enterprises of ownership by the whole people) have not fully accomplished financial independence; the price system has not been ironed out; the socialist market system remains incomplete and imperfect, and still in its development, while the macrocontrol means are in the same condition; hence, further exploration in the specific form of linking planning to the market is involved.[99]

To implement reform in the 1990's, China would not only issue its Eighth Five-Year Plan (1991-1995), but would adopt a Ten-Year Plan as well. The general goal would be to establish a "new socialist planned commodity economic system," and an economic operation mechanism which "integrates the planned economy with market regulation."[100] With that goal in mind, the Chinese would implement five main tasks:

1. Establish an ownership system with socialist public ownership as the predominant force and diverse economic sectors developing alongside.

2. Establish a system of enterprises that will suit the development of a large-scale socialized production. Except for a small number of noncompetitive enterprises, all enterprises should become competitive enterprises with the capacity for self-management, responsibility for profits and losses, self-development, and self-restraint. They should become commodity

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[99] *Ta Kung Pao* in FBIS, January 8, 1991, p47.

[100] *Renmin Ribao* in FBIS, March 20, 1991, p50.

producers and dealers, imbued with vigor and vitality and operating according to standard procedures.

3. Establish a unified and open socialist market system with complete rules and regulations for fair competition. The prices of a few important commodities and services vital to the national economy and the people's livelihood will continue to be set by the state. Meanwhile, production and circulation of other commodities will be open and subject to market regulation under the guidance of planning.

4. Establish a two-tier macroeconomic regulation and control system at the central, provincial, autonomous regional, and municipal levels which combines direct and indirect regulation and control, with indirect and the central authorities' regulation and control as the main forms.

5. Establish a system for distributing individual incomes, with distribution according to labor as the main body supplemented by other distribution methods, and a social security system.[101]

The new plans are strikingly similar to the reforms discussed in Section II above. The main difference is that now the Chinese want a slower pace. In discussing the new plans Li Peng remarked that China wanted to maintain the rate of growth around six percent.[102] This is primarily to avoid the inflationary tendencies of past reforms.

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[101] Ibid., pp50-51.

[102] *Ching Chi Tao Pao* in FBIS, March 21, 1991, p32.

Another difference in the "new" reforms is the priority given to large projects. Earlier, it had been noted that reform stressed small to medium industry, though actual statistics may have proved otherwise. This time, however, the Chinese are making large enterprises a priority. For example, 550 billion yuan has been earmarked for 10,000 projects for the Eighth Five-Year Plan, 62 of which are for retooling industries. This is a 38.4% increase over the amount provided to large industry in the Seventh Five-Year Plan.[103] Upgrading technology of current and new enterprises is even given priority over projects improving China's infrastructure. Apparently, China feels more than ever that the production of quality goods for export is *the* goal.

In fact, China has gone so far as to set up "Technology Zones" which are similar to the SEZ concept.[104] The government is allocating 1.7 billion yuan to facilitate the construction of fundamental facilities of these new zones. Enterprises established in the zones will receive the same preferential treatment as the SEZ's in that they are exempted from taxation for the first three years, and their tax rate will be 15% in the subsequent three years; if the export of an enterprise's products can reach a certain level, its tax rate can be further reduced (specific level not given).

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[103]Beijing Domestic Service in FBIS, April 12, 1991, p19.

[104]*Wen Wei Po* in FBIS, April 12, p42.

As mentioned earlier, the other avenue the Chinese have pursued to obtain technology is through foreign investment. To enhance foreign investment the Chinese promulgated the PRC Income Tax Law (Draft) on April 2, 1991.[105] This new law provides for single proportional tax rates providing easier understanding of taxes; the rates have been lowered to 33%, with a minimum rate of 15%; special cuts for foreign-invested enterprises in State-Council-designated areas up to 15% as long as they invest in energy, traffic, port, and harbor development or the construction of other projects encouraged by the state; and more strict enforcement of the law (i.e., violators will be punished).

There have also been moves toward greater price reform. The State Administration of Commodity Prices has decided that a major goal of the Eighth Five-Year Plan is to reduce control over prices. The main reason is to reduce the number of goods subsidized by the state, which amounted to 22.45 billion yuan in 1990 alone.[106] This has created a considerable drain on central funds. Furthermore, price increases should not exceed six percent annually in order to keep pace with the intended rate of growth and to avoid inflation. The primary commodities to have increases are in petrol, coal, and transportation in order to spur development in those areas. Food

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[105] *Renmin Ribao* in FBIS, April 15, 1991, p28.

[106] *South China Morning Post* in FBIS, April 24, 1991, p30.

prices will also be increased in order to pay for the cost of production.

A final indication of continued reforms is China's vehement opposition to the possible loss of MFN status with the U.S. This should be seen as a crying out for continued technology and contacts to push modernization forward. Of course, their definition of modernization is different, and their goal is different. None the less, it demonstrates the desire to open up to Western influences. All in all, the Chinese leadership seems determined to carry on the modernization of China.

B. HINTS OF RETRENCHMENT

Even though there are signs that China wishes to continue its modernization program, including the open door policy, there are also recent signals indicating economic as well as political retrenchment. For example, the China Survey Service, using 30 'experts' to conduct an economic resources study which began three years ago, issued an adverse report. It said that based on China's huge aging population, poor resources and infrastructure, and decreasing arable land, an "appropriate method of development" should be adopted instead of current plans: "Based on the conditions it analyzed, the report suggested an *unconventional* approach towards modernization, in which the traditional high speed economic

increase oriented strategy is replaced by the one emphasizing on consistent, *coordinated* development (italics mine)."[107]

Unfortunately, the leadership always stressed a steady growth rate in the past; neither too fast or too slow. The remark "traditional high speed growth" might indicate that the PRC is intent on limiting foreign investments. This would be consistent with trying to eliminate corrupting elements from foreign society. It may also be an attempt to warn the domestic population that future growth may be slow in light of the international sanctions being imposed.

The other two key words are "unconventional" and "coordinated." It is most likely that unconventional refers to some new approach to reform, though it is too early to tell what that may be. "Coordinated," on the other hand, most likely indicates increased centralization, at least in the short term. Thus, it seems like "Tiananmen" has had an immediate impact on China's economic modernization, but their continued demands for loans, capital investment, and Most Favored Nation status would imply that certain aspects of modernization continues.

Other aspects that will be discouraging to the U.S. is how the Chinese treated the Tiananmen massacre and other ideological rhetoric since June, 1989. For example, a Xinhua release, referring to the secret Scowcroft visits, completely downplayed the Tiananmen incident. Mostly stating approval of the visits, the article made only

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[107]"Conditions Termed 'Unfavorable' for Modernization," FBIS July 30, 1990, 36.

one remark regarding the bilateral relationship: "The two sides also discussed Sino-U.S. relations," and, "solving as soon as possible the disputes on some problems between the two countries since last June, so that Sino-U.S. relations can enjoy a new development."[Ref. 92][108] It would appear that human rights continue to be a low priority in China. Another warning sign that was ignored in the past was socialist rhetoric. Considering the unfolding of events, however, it is wise to take notice of them. Thus, the statement, "As a Communist, I am convinced that socialism will triumph in the end,"[109] from Jiang Zemin, the current Party General Secretary, may be an important factor in determining how to proceed with China.

The most notable restriction to continued reforms will be the pace of reform including the emphasis on stability. This is a direct link to the events in Tiananmen in 1989. The main argument is that an unstable China is adverse to the people's human rights (those of having food and a decent standard of living) and the rest of Asia and the world. The principle of stability is noticeable in most speeches on reform. For example, Qian Qichen, China's Foreign Minister remarked:

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[108]*Xinhua* in FBIS, December 11, 1989, pp1-5.

[109]"Jiang Zemin: 'Incident' 'Much Ado About Nothing'," FBIS, June 6, 1990, 7.

We shall continue to carry on the reforms and the opening up-policy. We so this only according to China's own conditions and for the Chinese people's benefit, and we do not plan to copy any foreign model...If some people try to impose their social system and values on China, they will never be accepted by the Chinese people.[110]

Perhaps more disheartening for human rights advocates in the U.S. was an article that referred to Deng's recent views on China's situation:

To grasp this opportunity, China must stress stability. Only when China has stability, reform, and opening up, can it go on developing...To be stable, China must have a core, which is adhering to the four cardinal principles.[111]

The four principles of upholding the leadership of the Communist Party (preserving the general structure of state, following a socialist course in economic development, and maintaining Marxism as the official ideology) can only imply that the current leadership wishes to continue on its present path. In other words, modernization remains socialist and future demonstrators can expect the worst.

Another unfortunate prospect is the possibility that state planners are thinking about recollectivizing state agriculture to increase grain production.[112] Despite the record harvest in 1990 of

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[110] *Renmin Ribao* in FBIS, October 10, 1990, p5.

[111] *Wen Wei Po* in FBIS, June 18, 1990, p30.

[112] *South China Morning Post* in FBIS, March 21, 1991, pp41-42.

435 million tonnes of grain China still had to import 15 million tonnes to feed its people. Estimates indicate 520 million tonnes will be needed by the year 2000. Therefore, by limiting the scope of the responsibility system and using collectives the state would have more control over what is planted. Furthermore, the collectives would facilitate the use of large agricultural machinery and potentially increase output.

In summary, the Chinese wish to continue their modernization effort as described in Section II. In fact, most of the literature reveals much of the same type of discussions on reform, including the socialist character. It also appears that China's reforms will continue to be cyclical in nature, going into periods of retrenchment as the economy heats up and inflation and deficits pressure the "radical reformers" to succumb to hardliner pressure. The major addition to the new reforms is the six percent growth rate, and the continued references to maintaining stability (which was always there but now more apparent). Most importantly, the key to China's future lies within its leadership. As to which faction dominates after the older leaders pass away no one can tell; but it is that very question that is so crucial to future Sino-U.S. relations.

V. U.S. POLICY AFTER TIANANMEN

The immediate reaction to China's violent crackdown of the "democracy movement" was one of outrage, protest, and disbelief. Most countries responded with harsh rhetoric immediately following the massacre, but withheld imposing sanctions while waiting to see how events would unfold. Though the violence lasted only two days in the square itself, the PRC began a "vigilante" program, hunting down suspected instigators of the movement, and purging its own party of unwanted sympathizers.

U.S. policy after Tiananmen would consist of a number of sanctions imposed on China. The dilemma, though, was to what degree should they be carried to. President Bush, on the one hand, decided it was best not to isolate China totally through economic sanctions. On the other hand, Congress and many others, including Chinese students and American specialists on China, felt it advisable to impose heavy sanctions on China as punishment for their action. As a result of the opposing positions, U.S. China policy would be hotly debated in America.

A. THE PRAGMATISTS

The United States responded on June 5, 1989, by suspending all government to government and commercial sales of weapons to China, suspending visits between U.S. and Chinese military leaders, giving a sympathetic review of requests by Chinese students to

extend their stay in the U.S., offering aid via the Red Cross for the wounded, and reviewing the U.S.-China bilateral relationship.[113] President Bush did not, however, pose any economic sanctions at that time because he wanted to leave the option open while waiting to see if China's repressive policies would cease.[114] This did not happen.

With military sanctions imposed, President Bush tried to use economic sanctions to further influence China's leadership. With those, "in the bag," he attempted to get the Chinese Government to grant clemency for captured protesters sentenced to death and stop the search for those not caught. The attempt failed. China continued its repressive policies. In a hope to curtail China's policies the White House imposed further sanctions on China. These included the suspension of "high level" meetings between U.S. and Chinese officials, the indefinite suspension of $1.3 billion in international bank loans, opposition to liberalize COCOM restrictions regarding China, suspension of export licenses for U.S. satellites to be launched by China, and stalling implementation of the Sino-U.S. agreement regarding nuclear energy.[115]

The early U.S. response to Tiananmen was hopefully designed to prevent further repressive actions on the part of the PRC. The administration genuinely tried to help the Chinese people. But as

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[113] William McGurn, "Tiananmen Square," in The Broken Mirror, pp235-6.

[114] "President Spurns Other Sanctions," NYT, June 6, 1989: A1; 5.

[115] See NYT, June 21, 1989: A1;2, and also McGurn, p236.

time dragged on, and it became apparent that military sanctions, suspension of high level talks, and attempts to stop loans from going to China were not producing results, the administration had to develop a new strategy. In doing so, the administration would end up trying to establish a "base" from which to work. U.S.-Chinese relations were important. In the attempt to sustain the relationship, though, President Bush would end up carrying out actions appearing to oppose stated policy and, therefore, create an aura of inconsistency, confusion, and illusion. Critics in the Congress, and the general public would come to wonder what exactly U.S. China policy entailed.

The administration, particularly President Bush, never intended for Sino-U.S. relations to break apart. Though Bush demonstrated contempt for China's actions by claiming "we can't have totally normal relations unless there's a recognition of the validity of the student's aspirations."[116] United States policy towards China remained relatively normal. In fact, two days prior to that statement the United States was "engaged in diplomatic efforts" to correct the situation.[117]

One fear was that economic sanctions may do more harm than good. Such sanctions might actually hurt the people of China, those

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[116]Nicholas D. Kristof, "Relations With U.S. Seem Badly Hurt By Crushing of Democracy Protests," NYT, June 11, 1989: A16; 1.

[117]From transcripts of Bush News conference, Washington D.C., June 8, 1989, reprinted in NYT, June 9, 1989: A22; 1.

we wanted to help, more than its leaders. Another fear was that an enormous amount of sanctions might give Chinese hardliners ammunition to overtake the government. If this happened, Deng's reform movement would likely be halted. The United States would then have jeopardized an important relationship. As Michel Oksenburg, a China-watcher, put it, "at this moment of understandable emotional fury we have to remember the bigger picture."[118]

Furthermore, the administration did not want American private business to pay the price for sanctions. The "future involvement of American business in China could be influenced greatly by further economic sanctions imposed."[119] In other words, big business would lose money. Moreover, Americans would not only lose profits, but they would be lost to Japanese companies because the Japanese were not going to wait for China's human rights policy to improve in order to continue doing business. For example, the U.S. granted a waiver to Boeing Industries allowing an airplane contract to go through to China. According to administration officials, "the decision to grant the waiver was made by Secretary of State James A. Baker 3rd and was coordinated with the White House." When the officials were

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[118]Michel Oksenburg, "Confession of a China Watcher," Newsweek, June 19, 1989, p30.

[119]Richard W. Stevenson, "Companies Hesitating on China," NYT, July 3, 1989: A25; 6.

asked if President Bush knew about it, they replied: "I'm sure he's aware of it."[120]

The administration would also seek to "soften or eliminate the sanctions against China voted by Congress," that occurred in late 1989 (see Moralist section below). It was time that "human rights stop driving our foreign policy."[121] Instead, U.S. national interests should dictate policy. The administrations decision to continue talks with Beijing about closer trade relations reflects the conviction that such talks serve both countries long-term interests.[122] Here we begin to see the overriding concern. Though human rights are an important part of U.S. foreign policy, they are not the only concern. Other interests, such as trade, must be considered.

Though Congress would be quick to criticize Bush's China policy, the President had many outside supporters. A lobby of well known businessmen prompted by Richard Nixon urged a return to business-as-usual.[123] Henry Kissinger, in his syndicated column, argued that "China remains too important for America's national security to risk

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[120]Michael R. Gordon, "U.S. Grants Boeing Waiver To Deliver Jetliners to China," NYT, July 8, 1989: A1; 6.

[121]R. W. Apple Jr., "Reaction to China Reopens Old Battle," NYT, September 11, 1989: A16; 1.

[122]"Talk to China-Despite the Chill," NYT, September 16, 1989: A26; 1.

[123]Miles Kahler, "The Myopic New China Lobby," NYT, August 26, 1989: A23; 1.

the relationship of the emotions of the moment."[124] The importance of maintaining relations must outweigh the sentimental pleas for human rights. Even the Chinese wanted the relationship to continue. Foreign Minister Qian Qichen, when meeting with Secretary Baker, said: "the fundamentals of the relationship haven't altered."[125]

President Bush did not have to look far for help. In October, 1989, former President Nixon visited the PRC on a "fact-finding" mission. Openly criticizing the events in Tiananmen, Nixon still looked favorably upon U.S.-Sino relations. He would stress the importance of a continued relationship. It was time to move ahead. Both countries were hoping his trip would "smooth relations."[126]

Perhaps the most spectacular indication of U.S. foreign policy was the high level "secret" visit of the President's National Security advisor, Brent Scrowcroft, and the Deputy Assistant Secretary of State, Lawrence S. Eagleburger, to China in December, 1989. In a seemingly direct violation of stated policy not to have meetings between high level officials, the President secretly sent two of his closest advisors to China. This was not all. During the December visit it surfaced that both officials had visited Beijing in July, less than one month after the terrible massacre of Chinese demonstrators (it would

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[124]Henry Kissinger, "The Caricature of Deng as Tyrant Is Unfair," Washington Post, August 1, 1989: A21.

[125]Nicholas D. Kristof, "U.S.-China Falling-Out: Much Smoke But No Fire," NYT, September 30, 1989: A5; 1.

[126]See NYT, October 29, 1989: A11; 1.

be found out later that this occurred on or around July 4, Independence Day).

According to some administration officials the purpose of the December visit was to send "a political signal that we are now ready to resume relations on a more normal basis."[127] However, Bush contradicted this by stating: "To those suggesting that I have normalized the relationship with this power because of one visit, they simply are wrong."[128] Bush further confused the situation by suggesting that it wasn't the time to remove sanctions. Why had he been granting waivers if sanctions should not be removed? Obviously, the President was trying to play down the visits. Shortly after the Scowcroft-Eagleburger embarrassment, and the statement that sanctions were not removed, Bush continued "normalizing" relations by waiving a "Congressional ban...on loans to companies that do business with China." He also approved the "export of three communication satellites" to China. This, of course, was not favoritism towards China, but was "in the national interest of the United States to approve export licenses."[129]

The next step towards "normalization" came in the form of China's removal of martial law from Beijing on January 10, 1990. Not

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[127]"China Trip Seeks to Alter Americans' Perceptions," NYT, December 10, 1989: A23; 1.

[128]Maureen Dowd, "Bush Defends China Visit," NYT, December 17,1989: A32;1

[129]Andrew Rosenthal, "President Waives Some China Curbs," NYT, December 20, 1989: A1;4.

missing a beat, the U.S. immediately announced that it was easing blanket opposition to World Bank loans to China.[130] President Bush announced that $780 million in World Bank loans that had been withheld would be reexamined on a case by case basis. It was emphasized that only "basic human needs" loans would be approved, as opposed to "project" loans. Shortly thereafter, the U.S. Export-Import Bank approved a $9.75 million loan for the China National Offshore Oil Company to purchase oil equipment and machinery.[131] Three days later the Ex-Im Bank approved another $23.1 million for the Shanghai Transport system, and the World Bank provided $30 million for earthquake relief.[132] Apparently, basic "human needs" loans were broadly defined.

China's lifting of martial law in January, 1990, had a salutary effect on American policy. Only a month later, though, the administration continued to confuse people by voiding a sale of plane parts to Beijing. On February 2, 1990, Bush nullified the sale of airplane parts by Mamco Manufacturing Company to a military related agency (China National Aero-Technology Import and Export Corporation) of the PRC. An eight agency task force said the parts

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[130]Robert Pear, "U.S. Easing Curbs As China Declares Martial Law Over," NYT, January 11, 1990: A1;6.

[131]Clyde H. Farnsworth, "Ex-Im Bank Resumes Aid to China," NYT, February 6, 1990, D1:3.

[132]Clyde H. Farnsworth, "China Wins Two Loans Backed by U.S.," NYT, February 9, 1990, A3:4.

involved sensitive materials and should not be sold to the PRC on National Security grounds.[133]

Though it appeared to contradict Mr. Bush's policy towards China, it was not clear whether either the World Bank loans or the plane parts sale signaled a change in that policy.[134] Finally, to put a cap on the entire response to the Tiananmen massacre the State Department, in February, issued the harshest criticism yet towards China, stating that China had "pervasive, severe violations of human rights in Beijing, Tibet, and other parts of China last year."[135]

The current debate in Sino-U.S. relations has turned once again to the issue of MFN. Before the June 3, 1991, the deadline for Bush to certify to Congress that China's emigration policy was satisfactory, the President announced his decision to grant the extension to China. Shortly afterwards, the President announced that the U.S. was imposing three new sanctions on China, including the blocking of computer technology that applies to missile tests. Though the administration denies it, many consider this a ploy to make Congress more amenable to granting China MFN status.

Basically, however, the same arguments discussed in Section III on trade restrictions still apply. The Chinese people, including Hong

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[133]Susumu Awanohara, "China card shuffled," FEER, February 15, 1990, p13.

[134]Andrew Rosenthal, "Bush Citing Security Law, Voids Sale of Aviation Concern to China," NYT, February 3, 1990: A1;5.

[135]Robert Pear, "U.S. Report Accuses China of Grave Rights Abuses," NYT, February 4, 1990: A26;3

Kong, along with the American consumer are apt to be the most affected by denying MFN status to China. It also seems unlikely that Congress will develop enough votes to override a Presidential veto if they pass a bill that links MFN to human rights in addition to emigration policy. Thus, as in 1990, China will retain MFN, Congress will complain for a brief time, and it will fade away as the fiscal year nears its end and budget considerations dominate U.S. politics.

The entire course of events from June 4, 1989, to the present have been designed to maintain normal relations with the PRC. President Bush had difficulty dealing with the tremendous outpouring of protest, both in Congress and publicly, towards the events the Chinese Government chose to pursue in Tiananmen. While trying to satisfy public outcry to punish China he also chose to satisfy the Chinese Governments' desire to maintain good relations with the United States. While stating that relations would not, could not, be normal between the United States and China, his actions as an administrator kept relations as normal as they could be. But why create contradictory policies that could potentially jeopardize America's reputation in order to maintain ties with an openly repressive government in China? The answer depends on how one views U.S.-China relations.

Susan L. Shirk, in a Foreign Policy article, wrote that how we estimate the degree to which U.S. interests are at stake in the relationship and how we evaluate the fragility of the relationship will determine whether or not the administration is right to treat

China as an exception to America's human rights policy.[136] She was talking about the Carter administration then, but the same view could be applied to Bush's policy on China. The point is that if the relationship is weak, we should be careful with policy that may jeopardize that relationship, as long as the relationship fulfills U.S. interests. Apparently, even after the June massacre the Bush administration felt that continued U.S. relations with China was in the national interest. Harsh economic and political sanctions against Beijing would perhaps have put that relationship back twenty years, to the pre-1972 position.

The United States needs China as a possible counterweight to Soviet aspirations in Asia, and needs China also to remain relevant in Japanese eyes as a key shaper of Asian events.[137] This statement by Henry Kissinger in August of 1989 was made prior to the reduced East-West tensions that resulted from Gorbachev's acceptance of events in Eastern Europe in November. However, it underlies one former theme guiding U.S. policy in Asia: that of countering the Soviet threat. Hence, one possibility for Bush's insistence on maintaining relations is geopolitical. From June until the fall of the Berlin Wall one main concern that U.S. sanctions might do was to drive the Chinese into Soviet arms. This would possibly have put the

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[136]Susan L. Shirk, "Human Rights: What About China," Foreign Policy, No. 29 (Winter 77-78): 109-127.

[137]Kissinger, "The Caricature of Deng," A21.

strategic balance on the side of the communists, and weaken the relative strength of NATO. This concern now has disappeared.

During the protests in May 1989, while Mikhail Gorbachev was in Beijing, there was even the fear that "for free nations, the Sino-Soviet rapprochement is not a net plus."[138] U.S. policy towards China during and after the protests may have been designed not to antagonize the Chinese. Yet Bush stated he was not worried about the improvement of Sino-Soviet relations. Does this mean President Bush was not concerned about the strategic balance? After November of 1989 U.S.-Soviet tensions were reduced. However, the Soviets had created a new political influence in Asia not seen before. Was this new Soviet political influence possibly a greater threat than the military threat? Or does the U.S. have other interests in China? Lawrence S. Eagleburger, Deputy Secretary of State, would argue in February before the Senate Foreign Relations Committee, that China's strategic value had not been diminished by the reduction in U.S.-Soviet tensions, but the emphasis of China's strategic importance had shifted to other problem areas such as global pollution, weapons proliferation, Cambodia.

China is a country of great importance for it influences stability in Asia. Outside pressures will almost certainly strengthen conservative

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[138]William Safire, "The Long Demarche," NYT, May 18, 1989: A31;5.

hardliners and weaken moderate reformers.[139] The concern may have been that continuing sanctions after Beijing lifted martial law would favor hardliners. The reforms achieved over the past ten years would then be considered useless. The result may be tension in U.S.-China relations. The U.S. could lose potential influence over an important Asian nation. It also seemed that not all hope for reforms was destroyed at Tiananmen. For example, China had readmitted a correspondent for Voice of America into the country, the possibility of a Peace Corps program was being talked about, and they had supported the United State's in the Gulf conflict. As Lawrence Eagleburger put it: "The forces favoring reform have not disappeared."[140]

The business world also looked to China to satisfy American interests in trade. The United States could lose a large potential market. There are big opportunities in China, and America can not afford to lose the market to the Japanese, the Germans, or anyone else.[141] The United States also has other interests in China. Politically, it was a big country in a vital area. One of growing importance. And China has influence over its neighbors. China is

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[139]Doak Barnett, "Increasingly, Bush Seems Right on China," NYT, January 21, 1990: D21;1.

[140]Robert Pear, "U.S. Official Urges 'Real World' View of China," NYT, February 8, 1990: A17;1

[141]Adi Ignatius, "Bush's Brother, Other Americans Are Talking Business With China," Wall Street Journal, September 18, 1989: A12.

also a military power and, therefore, must be reckoned with. Finally, the economic interests in China are great. U.S. policy cannot cause the doors to be closed. Sanctions could also result in China's withdrawal inward.

The most comprehensive and thought-out reasons for the administrations policy were presented by Eagleburger before the Senate Foreign Relations Committee. As he put it:

> This is a long-haul situation. It will take a good bit of time. We are hopeful, but can certainly not guarantee that the process we are now following will, in fact, lead the Chinese Government toward reform and democratization, economic and political.[142]

Furthermore:

> The issue is how best to transform rhetoric into reality. Do we see[k] to isolate China and cause it to turn inward or do we seek to facilitate its return to reform and openness by continuing to pursue the contacts and ties that encouraged such reform in the first place.[143]

Finally, one interesting point Eagleburger brought out, was that reform in China must occur from the top down, whereas in Eastern Europe, the reform movement had a widespread grassroots base at the bottom. Surprisingly, Senator Biden responded, "Quite frankly, that is the only remotely sound explanation for your policy."[144]

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[142]Robert Pear, "U.S. Official Urges 'Real World' View of China," New York Times, February 8, 1990, pA17.

[143]Eagleburger's testimony before Congress, Senate, U.S. Policy Towards China, p7.

[144]Ibid., p47-8.

Eagleburger would also argue that China's releasing of detainees and ending martial law, and the other steps that they had taken, were at least an earnest, to some degree, desire on the part of Beijing to "begin to change the relationship and to begin to undo the steps that they took at the time of Tiananmen Square."[145] Furthermore, Eagleburger states that during the first (July) visit the Chinese were cold; they did not really react to the talks, but just listened. However, during the second visit (December), Eagleburger sensed a slight breakthrough. As he put it, "there was a much better give and take back and forth" the second time.

However, for the short term, China's human rights violations overshadowed other U.S. interests in China. As a result, Congress would be more reluctant to allow presidential waivers to go through. The "post-Tiananmen" Chinese leadership would vehemently oppose the economic sanctions and the threat of losing MFN from Congress. They would argue that China's loss of MFN would harm U.S. consumers and businesses. Inexpensive Chinese goods would no longer be available, the Chinese market would be closed to the U.S., and investment opportunities would be lost.

While taking the pragmatic approach, Bush must also keep in mind the opposition. Totally to ignore the "moralist" attitude toward China could politically backfire. In a way, Bush has already done this. He imposed sanctions immediately after the incident. Though

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[145] Ibid., p27

he vetoed a Congressional bill to allow Chinese students to remain in the U.S. the President achieved the same goal through administrative means. The state department has issued incriminating documents on China's human rights abuses. Technically, sanctions remain in affect, and three new have been imposed recently. Thus, President Bush's policy has tried to balance both the aspect of maintaining U.S. values while trying to pursue U.S. interests.

B. THE MORALISTS

As mentioned above, President Bush's apparent "complacency" towards the repressive Chinese Government was bitterly opposed by some members of Congress. They attempted to make economic sanctions into law passing a resolution 81-10 in the Senate, and 418-0 in the House.[146] The opposition to Bush's China policy would continue. Congress was outraged by the PRC's actions in June. They were even more concerned with the course President Bush was taking. The tensions would become worse as time went by.

Events took a turn for the worse when Congress passed a bill extending visas for 40,000 Chinese students in America. This became more of a battle between the administration and Congress, over means to an end, but one that ultimately effected the Chinese Government. The President, stated that he had sufficient power to achieve the same objective administratively as the Bill did legally.

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[146]See NYT, July 15, 1989: A2; 4.

Beijing urged the President to veto the Bill or else they would stop all student-exchange programs.[147] The Bill was vetoed. In January of 1990 the House overrode the veto, 390-25. However, the Senate failed by four votes to get the two-thirds majority needed to override the veto.[148] Bush had won a major battle. He maintained his political power. More importantly, he kept the making of foreign policy in the executive branch of government (many felt this was a defeat for human rights). Yet if the President achieves the same objective as Congress where's the loss? Both sides gained: The President was reaffirmed in his direction of foreign policy and Congress had its voice heard in complaints over China's action.

The secret visits by General Scowcroft and Secretary Eagleburger were particularly troublesome to some Congressmen. Apparently, the U.S. could send top advisors to China without having normal relations, and Presidential waivers did not "lift" sanctions. In his attempt to show firmness towards the Chinese Mr. Bush confused everyone. The trip was considered a double standard policy favoring the Chinese at the students' expense. Would we have done the same if it were the Soviets? Was President Bush "kowtowing to the Chinese Government?"[149]

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[147]Robert Pear, "Bush Rejects Bill on China Students," NYT, December 1, 1989: A24; 3.

[148]Thomas L. Friedman, "Lobbying Effective," NYT, January 26, 1990: A1; 6.

[149]Elaine Sciolino, "President Defends Aide's China Visit," NYT, December 12, 1989: A9;1.

Not only has there been a large controversy over China's MFN status and GATT membership, but the "trade wars" continue. In late December, 1990, the U.S. slashed China's quota's in key garment and textile categories by half-million dozens.[150] The U.S. accused China of evading quotas by using fraudulent country-of-origin certification. There could also be a further one million dozen cut do to ongoing investigations. Finally, the U.S. claims a $12 billion deficit with China, second largest after Japan.

The issue of slave labor has also been raised in the MFN debate. Congressional critics of Bush's policy indicate that those Tiananmen demonstrators captured and punished are now being used to make cheap products for export to the U.S. Chinese leaders have repeatedly denied the accusations, stating that PRC law prohibits the export of goods made from convict labor. Technically, if one pushes the point, it could be argued that all labor in repressive, socialist regimes, is slave labor. Therefore, no goods should be imported from socialist countries. Some question the wisdom of basing U.S. foreign policy decisions on such a matter as this.

Thus, there are many critics of Bush's policy concerned with the current course of U.S. China policy. Foremost is the "double standard" of human rights. As mentioned earlier, would the United States have reacted in similar fashion had the Soviet Union killed thousands of its people in Red Square? Is Tibet different from Kuwait? The U.S. has

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[150]Carl Goldstein, "China needles U.S.," FEER, January 24, 1991, p35.

funded rebels in Nicaragua to overthrow a totalitarian government. In November, 1989, U.S. troops entered Panama searching for Noriega, captured him, and put into power a leader who stood for "democracy". Is it because China is so far away that we did not react more harshly? The United States helped to oust Marcos from the Republic of the Philippines for imposing martial law and severely repressing the Filipino people. It seems, then, that Washington applied "a different set of standards and expectations to China than to most other nations."[151]

Duality of standards will tend to weaken U.S. credibility in the near future. Nations will have a difficult time believing what the U.S. says. Instead, other states will have to ignore U.S. statements and wait for actions. This could be dangerous. The U.S. may find that threats no longer produce results. Instead, the U.S. might actually be forced to carry out actions when that may not be desired. The concept of deterrence is based on the principle of credibility. United States' China policy may have reduced U.S. credibility. Current policy may also give other nations, especially North Korea, Vietnam, South Africa, and other totalitarian and repressive governments, more leverage when dealing with the United States concerning human rights issues. They will be able to attack our stand on "high morals." They would be able to point and say, "you do not stand for

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[151]Marie Gottschalk, "The Failure of American Foreign Policy," World Policy Journal, Vol. 4, No. 4(Fall 1989): 667-684.

human rights except in isolated cases." Instead, current policy indicates that what Americans are really concerned about is geopolitical stability and trade. This is not good for the credibility the United States desires.

Domestically, President Bush's credibility was reduced due to the secret meetings between Scowcroft-Eagleburger and Beijing. The administration lied. While high level meetings were legally suspended, some high level meetings were actually occurring. The Iran-Contra affair took place not more than five years ago, when George Bush was Vice President of the United States. Does this mean that a President can lie to America and the world to achieve what he claims is in the American national interest? Lying compounds the already stated problems. Lying to the people and Congress hurts future policy. The president may have lost much of the trust and respect of the American people. Without those qualities it will be harder for the administration to create public support for other policy issues.

Granted, the American public forgets fairly quickly, but Congress does not. They tend to harbor grudges. The Scowcroft trips will not be forgotten. President Bush will have a much harder time lobbying support in Congress for controversial foreign policy decisions, such as Most Favored Nation status for China, or the Soviet Union. The meeting between China's Foreign Minister, Qian Qichen, and President Bush, at the White House in November, 1990, was criticized. Had the

U.S. made a deal with China on the U.N. resolution permitting the use of all means to get Saddam Hussein out of Kuwait?

In order to quell the Congressional uproar China released over 900 political prisoners in 1990, lifted martial law in Tibet, released Chinese dissident Fang Lizhi and his family, and voted favorably(or abstained) on the U.N. resolutions regarding Iraq's invasion of Kuwait. Though these were considered steps in the right direction Congress was still intent on voting against MFN. However, Congressional leadership failed to meet an October 18, 1990, deadline to cast a vote on the issue. As a result, China maintained its MFN status until June,1991, at which time President Bush certified its extension.[152]

Surprisingly enough, while President Bush was supporting MFN for China he was denying MFN for the Soviet Union because of the recent turmoil in the Baltic Republics.[153] This did not set well with Congress:

> The President's position is completely inconsistent. That's what happens when you have a policy based on expediency rather than principle.[154]

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[152]See Awanohara, "Rights or duties?" and Awanohara, "No more favours."

[153]R. W. Apple, "Bush Withholding Normal Trade Ties From The Soviets," New York Times(NYT), May 25, 1990, A1:6.

[154]Ibid.

The President defended his position by stating that the sanctions on China "remain basically unchanged," and that "trade would drop, drastically hurting exporters, consumers and investors."[155] One critic argues for a harsher economic policy. Since trade with the West is critical to China's modernization of both its economy and armed forces, continued dealings with China will only strengthen the hands of the authorities.[156] Moreover, the U.S. should ensure that China's entry into GATT is consistent with the rules, linking membership to such "market-opening measures as free pricing, copyright guarantees, and so forth."[157]

Two questions come to mind; if Congress was so opposed to granting China MFN why did they miss the deadline? and how big a loss is it if the U.S. were to lose less than one percent of its total world trade and about 1.5% of its world investments?

In summary, it is possible that President Bush has done a credible job of maintaining a delicate relationship, vital to world stability, despite an inhuman event. Other nations appreciate the fragility of any foreign relationship with China and understand that China is a country adverse to foreign interference. Most nations share the President's opinion that to create a more stable world,

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[155]"Excerpts From Bush's News Session on China's Trade Status With U.S.," NYT, May 25, 1990, A12:1.

[156]McGurn, p238.

[157]Ibid., p243.

especially in Asia, requires the participation and cooperation of China. Therefore, Bush's approach to China may have been well thought out in responding pragmatically instead of emotionally. His policy may have contributed to an increase in credibility and to the promotion of peace and stability in the Asian-Pacific region.

On the domestic scene Bush's policy though criticized openly by some may be applauded inwardly by others. Americans may conclude that Bush really could not do otherwise than he did without jeopardizing a permanent relationship. More importantly, Congress may acquiesce in his point of view although as a democratic body it has to oppose controversial policies of a Republican President. The people expect it.

VI. CONCLUSION

Sino-U.S. bilateral economic relations have grown substantially since the normalization of relations in 1979. One of the most important factors in this growth has been China's modernization. Even though the relationship has developed positively over the past twelve years there have been conflicts.

Since the Chinese began agricultural reforms in 1978, substantial progress has been made. The adoption of the household responsibility system, greater autonomy for the peasants in decision making, and price flexibility, created new incentives for increased productivity. Unfortunately, inflation and poor infrastructure caused a slowdown in this productivity to the point that without further relaxation of prices and central planning the high growth rates of the early to mid-1980's would have been impossible.

Industrial reform measures produced significant results for the average worker. Greater autonomy for enterprises, price reform, and the opening of coastal cities for international trade and commerce improved China's standard of living. Yet the same obstacles that faced the agricultural sector impacted the industrial sector.

After Tiananmen, the forces for reform continued to exist. The Chinese leadership realizes that to continue modernization the help of the outside world, particularly the Western countries, is needed. In this sense, modernization will continue. However, it is in dealing

with the West, especially the U.S., that problems arise because of the tremendous difference in socio-economic systems.

This became apparent by the outrage expressed by the United States towards Beijing's crackdown of democracy demonstrators in Tiananmen square in June, 1989. However, the degree of outrage may have been due in part by U.S. policy-maker's own misperceptions of what China was really attempting to accomplish through modernization. The U.S. also failed to appreciate the extremes to which the Chinese Government would go to suppress challenges to its own authority.

In Section II it was argued that China's reform policies were not intended to transform China into a democracy or free market economy. On the contrary, it was shown that China's reform had always been geared to reform socialism. Market regulation, price reforms, opening up, and agricultural reform were all used in the attempt to produce a modern socialist country. It seems so simple, but "modernization" means just that; to provide China with modern equipment, management techniques, and technology, so they can improve the welfare of the people in a socialist way.

Perhaps when China indicated that reforms would also include the political system, Western democracies, especially the United States, got their hopes up. However, Chinese political reform was merely intended to increase the efficiency of the bureaucratic structure left over from the previous 4000 years without relinquishing any substantial control. It seems that the political

direction in the Soviet Union and Eastern Europe helped to fuel that hope. Tiananmen provided a temporary setback.

U.S. economic policies towards China have been mixed, as far as trying to help their modernization program. Trade has flourished to some extent, but has been marred by disputes over trade balances. That is, both nations feel that the relationship should be mutually beneficial and equal, but conflicts have arisen because of American restrictions on China's export trade. Until there is agreement on what exports should be applied to China's quotas, the problem most likely will remain.

In the areas of technology transfer and foreign investment both sides have made progress. However, until China can obtain the levels of technology desired from the U.S. it will continue to complain and/or seek similar technologies from other sources. The complaints from U.S. businesses(along with other foreigners) about China's policies concerning investment will most likely continue, too. It seems the greatest impact on China will be through continued dialogue on what the rest of the world considers normal business practices. U.S. investors should keep in mind that if the Chinese perceive their trade deficit to be too large they will take measures to discourage foreign investment until the deficit nears a balance. Furthermore, as long as the U.S. review process on dual-use technologies remains slow and complex, complaints from both the Chinese and U.S. businesses will continue.

Financial (or banking) issues are also related to this theme of equality and mutuality of benefit. It is the disparity between the developed and underdeveloped countries that frustrates China. The main issue involves protectionist measures on the part of the developed countries that hinder the others' development. Also linked to trade and technology, the lack of any official U.S. aid program for China, plus the United States' dominant role in the IMF and World Bank, does not help the situation.

Closely associated with equality and mutual benefit is China's concern over sovereignty and internal affairs. The disputes over MFN, economic sanctions in response to the Tiananmen incident, and regulations governing foreign direct investments and joint ventures are directly related to China's perception of sovereignty. The Qing Dynasty's inability to control foreign encroachment during the 19th Century has left an enduring impact on the Chinese. It is hard for Americans to relate to this phenomenon, but the Chinese have a greater respect for history, perhaps, than Americans. It should be remembered that the early rebellions in China during the latter19th and early 20th Centuries were rebellions directed towards foreign encroachment. Therefore, when the U.S. criticizes Beijing's actions towards its own people, and bases the granting of MFN or loans on such affairs, China will react harshly; in their eyes it is another way of foreigners attempting to control what goes on inside China. It is not difficult to appreciate China's point of view.

Thus, it appears that socialist modernization, equality and mutual benefit, and sovereignty, are concrete concepts that must be considered in policy formation. One does not have to agree with the viability of socialist modernization, nor believe that we should treat all nations equally, or that we should not meddle in China's internal affairs. But by realizing that these concepts will exist into the foreseeable future, one can better prepare for and predict the outcome of U.S. policies towards China.

A. RECOMMENDATIONS

The key to future U.S. policy considerations is to recognize that China's modernization remains, for the foreseeable future, with its socialist parameters. Realizing this, the U.S. can then determine if good relations with China are essential for its own national security purposes. Though the Soviet threat has diminished (and this is still arguable), China remains vitally important respecting global security issues that range from environmental damage to weapons proliferation. Furthermore, as long as the Chinese remain a permanent member of the United Nations Security Council it seems essential to maintain harmonious cooperation with China. The recent Gulf War could be an indication of things to come, and having China on the side of the U.S. will only help.

Currently, the most debatable aspect of Sino-U.S. relations is the granting of MFN. The President has announced that he will extend the waiver for another year (June 1991-June 1992). This is

beneficial to both countries. First, it will not exacerbate an already strained economic policy regarding China. The Chinese officials would only consider the loss of MFN as an attack on them, and a violation of their sovereignty. The problem lies within the United States itself. Granting China MFN in view of their record in human rights is anathema to many in Congress. To them, the United States appears to have a double standard. One way out is to pass legislation that removes the Jackson-Vanik amendment.

For those that argue the current policy only strengthens the hand of the hardliners there is also the fact that contacts initiate change. Though it cannot be proven, it would be safe to say that the knowledge of what is possible has a very strong influence on those Chinese who demonstrated at Tiananmen. The democracy movement in 1989 was, in part, a cry for an increased standard of living. Few such movements existed while China was economically isolated from the West.

Besides the MFN issue, U.S. trade policies should be altered. The continued pressure for protectionist measures is a hindrance to good relations. The U.S. practice of including re-exports from Hong Kong in China's quotas has created problems in the deficit question. However, the U.S. could keep two accounts, one including China, and one without. The purpose would be to begin an integration of Hong Kong into China's economy. Finally, the U.S. must move away from increased protectionist policies,.

Technology transfers to China are hindered by both sides. Without improvements in China's investment climate it is doubtful that American businesses would be flocking to China's shores to invest. On the other hand, the complex and often slow procedure for reviewing critical technologies should be reformed. One improvement would be to establish a concrete cutoff between the yellow and red zones. Another improvement would be to establish a precedent system in that when one technology is permitted to go through, similar technologies could use past cases for review. One approach would also be to allow technologies to be transferred within a specified time limit.

In financial areas, the U.S. should create an official aid program vis a vis China. This would not only provide aid to needed projects, but create another level of contacts that could influence China policy. It seems strange that for years the U.S. has not had an official aid program for one of its most important relationships. Furthermore, if the President has waivered MFN, it seems useless to waive World Bank and IMF loans to China on a case-by case basis. The U.S. should state its reasons and just remove the remaining sanctions. The political backlash would be no worse than what has already occurred.

What must be borne in mind is that the current leadership in China intends to maintain socialism as the dominant ideology, and there is no guarantee that after Deng Xiaoping has passed away, the resultant leadership will be any different. Even Hu Yaobang and Zhao Ziyang maintained that China would be "socialist" in character,

and there is no predicting the way in which "socialist" will be defined. Thus, U.S. policy must be formulated with this in mind; U.S policy must be flexible.

One must also decide the extent to which good relations with China are useful for U.S. national security. Even those critical of U.S. policy to date do not deny the need to maintain some sort of relations with China. The question is how to have the greatest influence on China, while realizing that any influence the U.S. have will only be slight. As Richard Nixon once said:

> The Chinese are a great and vital people who should not remain isolated from the international community...The principles underlying our relations with Communist China are similar to those governing our policies toward the U.S.S.R. United States policy is not likely soon to have much impact on China's behavior, let alone its ideological outlook. But it is certainly in our interest, and in the interest of peace and stability in Asia and the world, that we take what steps we can toward improved practical relations with Peking.[158]

The U.S. must, again, decide what is most practical for U.S. interests. The best way to improve economic relations is to keep the human rights linkage in perspective and help China modernize in its own preferred way. Only in this manner can the United States protect and promote its vital interest in China and in the entire East Asia and Pacific region.

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[158]Nixon's first Foreign Policy Report to Congress, February 1970, see Richard M. Nixon, The Memoirs of Richard Nixon(New York: Grosset and Dunlap: 1978), p545.

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